Equity and trusts

Robert Chambers
James Penner
William Swadling
Contents

1 Introduction ............................................................. 1
   Introduction ......................................................... 2
   1.1 Trusts: a difficult subject? ................................. 3
   1.2 Sources .......................................................... 4
   1.3 Learning outcomes, self-assessment questions and activities ................................. 5
   1.4 Advice on the examination ..................................... 6

2 Trusts – the basics .................................................... 7
   Introduction .......................................................... 8
   2.1 What is a trust? .................................................. 9
   2.2 Equity ............................................................. 11
   2.3 Comparison with other legal concepts ......................... 13
       Reflect and review ................................................... 16

3 Types of trust .......................................................... 17
   Introduction .......................................................... 18
   3.1 Express trusts .................................................... 19
   3.2 Discretionary, fixed and bare trusts ........................... 19
   3.3 The protective trust ............................................. 21
   3.4 Trusts arising by operation of law ............................. 22
   3.5 Resulting trusts .................................................. 24
   3.6 Testamentary and inter vivos trusts ......................... 25
   3.7 Purpose trusts: private and public (charitable) purpose trusts ................................. 25
       Reflect and review ................................................... 28

4 The express trust relationship ........................................ 29
   Introduction .......................................................... 30
   4.1 Introduction to rights and duties .............................. 31
   4.2 Powers and duties of trustees and others ...................... 33
   4.3 Typical administrative powers and duties ..................... 37
   4.4 Investment ........................................................ 37
   4.5 Power of delegation ............................................. 40
   4.6 Interests of beneficiaries and objects of powers ............. 41
       Reflect and review ................................................... 46

5 Creating express trusts I: the declaration of trust .................. 47
   Introduction .......................................................... 48
   5.1 Intention to create a trust ...................................... 49
   5.2 Identifying the rights .......................................... 52
   5.3 Identifying the beneficiaries ................................... 54
       Reflect and review ................................................... 60

6 Creating express trusts II: constitution ............................. 61
   Introduction .......................................................... 62
   6.1 Constituting a trust ............................................. 63
   6.2 Defective constitution ............................................ 64
       Reflect and review ................................................... 69
7 Proving declarations of trust and effecting dispositions of a beneficiary's interest under a trust .......................................................... 71
   Introduction. ............................................................................. 72
7.1 Proving a declaration of trust .................................................. 73
7.2 Transfer of equitable interests .................................................. 76
   Reflect and review. ..................................................................... 80

8 Secret trusts ............................................................................. 81
   Introduction. ............................................................................. 82
8.1 Will formalities ........................................................................ 83
8.2 Justifications for the admission of evidence of secret trusts ....... 85
8.3 Some specific issues. ............................................................... 87
8.4 What type of trust is ultimately enforced ................................. 89
   Reflect and review. ..................................................................... 92

9 Promises to create trusts ............................................................. 93
   Introduction. ............................................................................. 94
9.1 Promises in deeds ................................................................... 95
9.2 Promises for consideration .................................................... 98
9.3 Promises and detrimental reliance ......................................... 99
   Reflect and review. ..................................................................... 102

10 Purpose trusts I: public purposes ................................................. 103
    Introduction. ........................................................................... 104
10.1 Charitable status .................................................................... 105
10.2 The meaning of ‘charity’ ....................................................... 106
10.3 The public benefit requirement ............................................. 111
10.4 Contaminating non-charitable elements ............................... 113
10.5 Failure of charitable trusts: the cy-près doctrine .................... 113
    Reflect and review. .................................................................... 118

11 Purpose trusts II: private purposes .............................................. 119
    Introduction. ........................................................................... 120
11.1 Objections to private purpose trusts .................................... 121
11.2 The ‘beneficiary principle’ and the ‘no purpose trust’ rule ...... 122
11.3 Trusts for persons limited by a purpose ............................... 124
11.4 Anomalous valid private purpose trusts ............................... 125
11.5 Departures from the beneficiary principle ............................ 126
    Reflect and review. .................................................................... 128

12 Resulting trusts ........................................................................ 129
    Introduction. ........................................................................... 130
12.1 When do resulting trusts arise? ........................................... 131
12.2 Why do resulting trusts arise? ............................................. 135
    Reflect and review. .................................................................... 140

13 Rights ‘held’ by unincorporated associations ................................ 141
    Introduction. ........................................................................... 142
13.1 Gifts and other transfers to unincorporated associations ....... 143
13.2 The distribution of rights upon dissolution ........................... 145
    Reflect and review. .................................................................... 150
19 Constructive trusts II ........................................ 209
  Introduction ......................................................... 210
  19.1 Constructive trusts as a response to unjust enrichment ........ 211
  19.2 Constructive trusts responding to other miscellaneous events .... 212
  Reflect and review .................................................... 221

Feedback to activities ............................................. 223
Chapter 2 ............................................................... 225
Chapter 3 ............................................................... 225
Chapter 4 ............................................................... 226
Chapter 5 ............................................................... 228
Chapter 6 ............................................................... 229
Chapter 7 ............................................................... 230
Chapter 8 ............................................................... 230
Chapter 9 ............................................................... 231
Chapter 10 ............................................................. 232
Chapter 11 ............................................................. 234
Chapter 12 ............................................................. 234
Chapter 13 ............................................................. 235
Chapter 14 ............................................................. 236
Chapter 15 ............................................................. 237
Chapter 16 ............................................................. 237
Chapter 17 ............................................................. 240
Chapter 18 ............................................................. 241
Chapter 19 ............................................................. 242
1 Introduction

Contents

Introduction ..................................................... 2
1.1 Trusts: a difficult subject? .............................. 3
1.2 Sources .................................................. 4
1.3 Learning outcomes, self-assessment questions and activities ............................................. 5
1.4 Advice on the examination. ............................ 6
Introduction

The purpose of this subject guide is to help you study the law of equity and trusts. Working through this guide, you will gain an understanding of the subject sufficient to do well in the final examination. This is not, however, a matter of rote learning. Each chapter will introduce and take you through a programme of study, but it will not simply ‘give you the answers’ to be memorised for later regurgitation in the examination. Only by taking seriously the various instructions as to reading and answering questions will you attain the necessary grasp of the subject.

LEARNING OUTCOMES

By the end of this chapter you should be able to:

- appreciate why the law of trusts is considered to be a difficult subject
- identify the necessary sources of reading for studying this subject.
1.1 Trusts: a difficult subject?

The law of trusts is generally acknowledged to be one of the more difficult subjects in the LLB syllabus. This is mainly because of the nature of the trust which contains elements both of the law of obligations and of the law of property. In some ways, trusts are like contracts, and in other ways they mimic property relationships under the law. However, trusts are unique and it can be difficult to obtain an intuitive feel for the ways in which the law of trusts responds to particular problems. While you will certainly gain a feel for the law of trusts as you work through this guide, at times you may feel frustrated, and that you do not ‘get’ what the law is. Be patient and persistent. In particular, while you should work through only one chapter at a time, if you review previous chapters that you have already completed on a regular basis you will start to see how everything really does ‘fit together’. Consider each chapter in this guide as a piece of a puzzle. As you complete each chapter, you will add one more piece, and the whole picture will begin to take shape.

As with all LLB subject guides, this one is not intended to be a substitute for reading cases, articles and textbooks. The Essential reading and exercises set in each chapter must be taken seriously. Only by doing so will you obtain any genuine understanding of the law. Typically, the final examination will include as many problem questions as essay questions, and the only way you will be able to apply the law of trusts to new fact situations is to grapple with the reading and exercises and appreciate their demands.

Trust law cases

The main objective is to understand the principles laid down in the leading cases (as the law of trusts is primarily an area of judge-made law) and appreciate how statutes have modified, or codified, the law in the cases. As a general rule, the leading cases and important statutory provisions are those which are the focus of discussion in the relevant chapters in the textbooks.

A word about trust cases. Trust issues arise in all sorts of situations. The facts of trust cases often involve other areas of the law with which you may be unfamiliar, such as succession, taxation or commercial law. Not understanding these other legal issues can make it difficult to understand some cases. There is no easy solution to this problem, but what you must try to do is grasp the relevant trust law issue. You will better be able to do this if you approach the cases as follows:

- Start with the relevant section of the subject guide to give you an idea of the points to be looking for. Take one section at a time. Do not try to digest several in one go.
- Read the textbook passages about the case. This will generally describe the facts in such a way as to give a brief explanation of the surrounding law necessary for picking out the trust issues.
- Read the further reading or study pack readings recommended.

As to cases generally:

- When studying leading cases, take notes or re-read the cases so that you retain a grasp of what the case was about, how the judge approached the law, and what the decision was. Make a special effort to remember the correct names of the parties, the court which decided the case (particularly if it is a decision of the Supreme Court, House of Lords, Court of Appeal or Privy Council) and any other important features, such as the presence of dissenting judgments, the overruling of previous authority and apparent inconsistency with other cases.
- Read the textbook and subject guide passages again and ask yourself whether those interpretations of the cases agree with your impression of them. If they do not, read the cases again because you may have missed something or misunderstood it in some way. Also consider looking at another textbook. Different authors take different perspectives on the cases, and you might find another view more in keeping with your own.
In many areas of trust law the law is unsettled and there are cases going in different directions on the same issue. If this is so, be prepared to take a measured stance as to which is the better view of the law, and be prepared to defend your view of the cases, or the views of one author over another, in the examination. You will not lose marks for preferring one view of the cases or one learned author’s view over another’s, but it is important to show that you realise when the law is unsettled or that one particular author’s opinion is regarded as controversial.

Note that the vast majority of cases cited in this guide can be accessed through the Online Library.

1.2 Sources

The set textbook for this course is:


Detailed reading references in this subject guide refer to the edition of the set textbook listed above. A new edition of this textbook may be published by the time you study this course. You can use any recent edition of this book. Use the detailed chapter and section headings and the index to identify relevant readings. Also check the virtual learning environment (VLE) regularly for updated guidance on readings.

This book is essential reading for this course. It is an accessible and inexpensive shorter textbook which will introduce the topic of the chapter but at the same time discuss it in sufficient detail for you to gain a good sense at the outset of what the topic is about and the various difficult issues you will have to confront in order to master it. In view of this, the statement of learning outcomes which immediately follows will be comprehensible, and you will be able to begin to organise your thoughts about what seems to you straightforward in the topic and what will need concentrated effort to understand. In certain chapters, the Essential reading will also instruct you to revise one or more of the previous chapters of this subject guide. This does not mean, of course, that you should work through that chapter a second time, but it does mean you should spend at least half an hour going over that chapter and your notes and answers to questions to re-familiarise yourself with that topic. It is essential that you do this, so that you see the connections between chapters, and see how the different ‘pieces of the puzzle’ come together.

At the end of each chapter of this guide there is another section called ‘Essential reading’. This will always include pages from the other recommended textbooks (see below). It will also typically list cases and relevant statutory provisions. We have listed the relevant passages from three textbooks and you must read the relevant passages from at least one. You are advised to buy one of these textbooks, unless you have access to a good library that contains one or more of them. You will be aware that the different authors have different views and present the material in different ways, and some writing styles will be more accessible to you than others. So, if you can, examine some of the chapters in each book to find out which book is best for you.

Complete the Essential reading before attempting the sample examination questions at the end of each chapter, which have been written on the basis that you have done so.

The Essential reading is not the only reading available on the various topics covered and occasionally chapters may indicate some Further reading. These texts will broaden your knowledge of the chapter topic. At the end of each chapter of Penner, further reading is indicated, and you may use this as a guide for further reading where none is indicated in this guide. Do not attempt the further reading until you have tackled the Essential reading and have a solid understanding of the subject. Many of these texts are available through the Online Library, or in the study pack which accompanies this guide.
There are three other recommended textbooks:


In addition, the following, though not a recommended text, is an excellent collection of text and materials, to which you might usefully make reference:


*Note: detailed reading references in this guide refer to the edition of the textbooks listed above. If you are using a different edition of a textbook, you may need to refer to detailed chapter and section headings (as well as the index) to identify relevant readings.*

You are advised not to use any of the more down-market books on the subject, as they are not written at the level demanded by your Examiners.

**Statute book**
You should also obtain a statute book. Under the Regulations you are allowed to take one authorised statute book into the examination room.

Information about the statute books and other materials that you are permitted to use in the examination is contained in the current Regulations to which you should refer.

You are able to take into the examination one copy of one of the following books:

- **Blackstone’s Statutes on Property Law** (OUP), or
- **Core statutes on property law** (Palgrave Macmillan), or
- **Property law statutes** (Routledge).

Please note that you are allowed to underline or highlight text in these documents – but you are not allowed to write notes etc. on them.

Statute books are regularly updated: try to obtain the latest edition.

### 1.3 Learning outcomes, self-assessment questions and activities

A number of ‘learning outcomes’ are listed at the beginning of each chapter. The list is meant to be helpful. But be mindful of the fact that understanding any branch of law is not just about acquiring knowledge; you must learn to apply that knowledge, both to practical problems and to theoretical enquiries. In other words, you will be expected to be able to think about what you know and to write critically about it. That is why many of the learning outcomes are stated in the form of ‘knowing how’ to do something, or being ‘able to explain’ how the law in a particular area works.

To help you acquire this ‘knowledge’, you will come across activities, self-assessment questions and sample examination questions throughout this guide. It is important that you tackle these conscientiously. Doing so will help you to remember and understand the content of the course, and will also give you practice in writing legal English and formulating arguments that will help you when it comes to the examination.
Self-assessment questions require no feedback. They are designed for you to confirm
to yourself that you have identified and understood the issues which have been
discussed in the text. In addition to these questions, there are activities which usually
have some form of feedback. You can undertake all of these activities working alone,
but it is always useful to tackle questions with a group of fellow students if possible, so
as to promote discussion and debate.

Sample examination questions are included at the end of each chapter (except this
one); it is advisable to attempt to answer the question under mock examination
conditions (i.e. without consulting your notes or the text). Taking this approach will
help you develop your ability to think critically and construct a persuasive answer in a
limited time. It will also encourage you to review those areas where your knowledge
is insufficient so you cannot clearly and coherently answer examination questions.
On the other hand, you may find it more helpful to work through the questions with
your notes and books in front of you. The crucial thing, however, is that you get some
practice in writing examination answers before going into the examination itself.

**The structure of each chapter**

All the chapters follow a similar format, although some chapters may deviate from this
structure when certain more specialised areas of the law are considered. In general,
the chapter will contain, in this order: contents; introduction; Essential reading;
learning outcomes; the main text broken into the various sub-topics, in which are
interspersed self-assessment questions, learning activities with feedback, summaries
of material covered, and reviews of the learning outcomes; Further reading; and
sample examination questions with feedback.

### 1.4 Advice on the examination

**Important:** the information and advice given here are based on the examination
structure for the session 2015/16. We strongly advise you to always check both the
current Regulations for relevant information about the examination, and the VLE. You
should also carefully check the rubric/instructions on the paper you actually sit and
follow those instructions.

At the end of the course there will be an examination which takes the form of a three-
hour unseen paper. You will be required to choose four questions from a total of eight.
The choice is unrestricted in that there are no compulsory questions. The paper will be
made up of a mixture of essay questions, problem questions, and questions which may
combine elements of both. You should note that in an eight-question examination,
not every topic can or will be examined, and you should therefore not pin your hopes
on finding a question on a particular topic.
# Trusts – the basics

## Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction</td>
<td>8</td>
</tr>
<tr>
<td>2.1 What is a trust?</td>
<td>9</td>
</tr>
<tr>
<td>2.2 Equity</td>
<td>11</td>
</tr>
<tr>
<td>2.3 Comparison with other legal concepts</td>
<td>13</td>
</tr>
<tr>
<td>Reflect and review</td>
<td>16</td>
</tr>
</tbody>
</table>
Introduction

This subject guide is chiefly concerned with trusts, though other material will be encountered from time to time. Its essential aim is to enable you to answer the most common questions that could be asked about trusts. In this chapter, however, we will address a number of fundamental issues about trusts. The following chapters will then move on to examine the types of trust which can exist and the nature of the trust relationship (Chapters 3–4). After that, we will look at the requirements of a valid trust, considering issues of substance and constitution, and then evidential rules regarding proof of declarations of trust and substantive rules for dispositions of interests under trusts (Chapters 5–7). With that basic outline in place, we will then look at the specific topics of secret trusts, promises to create trusts, purpose trusts, resulting trusts and unincorporated associations (Chapters 8–13). This is followed by the administration of the trust, the appointment, retirement and removal of trustees, and variation of trusts (Chapters 14–15). We then turn to examine the equitable wrongs of breach of trust and breach of fiduciary duty (Chapters 16–17). Finally, we look at constructive trusts (Chapters 18–19).

In this chapter, we look at three things. First, what is a trust and why do people create them? Second, what is equity? And third, how do trusts differ from other related concepts? Understanding these topics is essential to understanding this whole subject.

Essential reading

- Penner, Chapter 1: ‘The historical origins of the trust’.

Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- explain in outline what is a trust, and why people create them
- explain the difference between law and equity and the role of equity in the enforcement of trusts
- explain how trusts differ from similar concepts.
2.1 What is a trust?

At its simplest, a trust is a device in which rights, either personal (e.g. a right to be repaid by a borrower) or proprietary (e.g. a fee simple or lease of land) are held by one person for the benefit of another. The person creating the trust is called the settlor, the person holding the rights is the trustee, and the person for whom those rights are held is the beneficiary.

2.1.1 Why create a trust?

We need to know why people create trusts. The question is perhaps answered by asking why someone might not want to give rights to another person outright (i.e. without the interposition of a trustee between that person and the right). There are a number of answers to this question, some of which are as follows:

First, a person could be incapable of managing rights. I might, for instance, want to give company shares to a child. Though there is no legal impediment to me doing so, such an action might be very foolish indeed, for the child may well have no idea of the value of what they have received. It is much better to give the shares to a trustee to manage on the child’s behalf.

Another reason is the flexibility trusts provide. For example, by the use of a discretionary trust (discussed in Chapter 3), funds can be released to those members of a class of potential beneficiaries who have the greatest need or the lowest tax liability. Indeed, tax management is often a reason behind the creation of trusts.

A third reason is that trusts can provide for the enjoyment of rights to be split on a plane of time. If I want my wife to receive the income from some investment throughout her life but to give the capital to my children, then the only way I can do so is by the use of a trust. This list is not intended to be exhaustive and there are other reasons why trusts are used.

REFFLECTION POINT

As you read trusts cases, make a note of the reasons for which the trusts were formed, if this is known. Consider what this tells you about the requirements for, and possible problems with, trusts law.

2.1.2 Trusts arising by operation of law

It is also the case that not all trusts are created by settlors. Sometimes, the law imposes trusts. These are generally known as either ‘constructive’ trusts or ‘resulting’ trusts. The reasons why such trusts are created are controversial and various, but it helps to have one or two clear examples at the outset. In Chase Manhattan v Israel-British Bank [1981] Ch 105, the claimant bank mistakenly paid US$2 million to the defendant bank. Although the defendant was personally liable at common law to repay the money, that was of little use to the claimant because of the defendant’s subsequent insolvency. Rights held by a trustee on trust for others do not form part of the estate available for distribution to creditors in the event of the trustee’s insolvency, and so the claimants argued for a trust. Goulding J held that when money is paid by mistake, the recipient holds it on trust for the payer, and so it came out of the insolvent estate. Another example of a constructive trust is that which arose in FHR European Ventures LLP v Cedar Capital Partners LLC [2014] UKSC 45, [2014] 4 All ER 79, [2014] 3 WLR 353. The claimants hired an agent to negotiate their purchase of a hotel unaware that their agent was also receiving a secret commission from the vendor. Since this was a breach of the agent’s fiduciary duty to loyally serve the claimants’ interests, the agent held that commission on constructive trust for the claimant.

Both cases are controversial and will be examined in detail later on. For now, they are simply given as examples to demonstrate that not all trusts are created intentionally by people who want to create them.
2.1.3 The juridical effect of a trust

There is some confusion with regard to the legal effect of creating a trust of a right. It is, for example, often said to involve the creation of a dual ownership, with equitable title passing to the beneficiary of the trust, and legal title to the trustee. However, the rights which the settlor had prior to the creation of the trust are vested in their entirety in the trustee. At the same time, new rights are created for the beneficiary of the trust, which enable the beneficiary to hold the trustee to account for the trustee’s exercise of those rights. The clearest discussion of this issue is to be found in the Australian case of DKL R Holding Co (No 2) Ltd v Commissioner of Stamp Duties [1982] HCA 14, 149 CLR 431. A company, 29 Macquarie (No 14) Pty Ltd, was the registered proprietor of a fee simple estate. It arranged with another company, DKL R Holding Co (No 2) Ltd, for the latter to hold the title in trust for the former once a change in registration was effected. The question was how much stamp duty was payable on the transfer to DKL R as proprietor. DKL R argued that only nominal duty was payable, since all that it received was the bare legal estate, with 29 Macquarie retaining the equitable interest. The argument was rejected in both the New South Wales Court of Appeal and the High Court of Australia. Speaking in the former, [1980] 1 NSWLR 510, 519, Hope JA said:

[An absolute owner in fee simple does not hold two estates, a legal estate and an equitable estate. He holds only the legal estate, with all the right and incidents that attach to that estate... Although the equitable estate is an interest in property, its essential character still bears the stamp which its origin placed upon it. Where the trustee is the owner of the legal fee simple, the right of the beneficiary, although annexed to the land, is a right to compel the legal owner to hold and use the rights which the law gives him in accordance with the obligations which equity has imposed upon him. The trustee, in such a case, has at law all the rights of the absolute owner in fee simple, but he is not free to use those rights for his own benefit in the way he could if no trust existed.

29 Macquarie did not therefore ‘retain’ an equitable interest; their equitable interest only arose on the transfer and the tax was therefore payable.

Similar views were expressed when the case reached the High Court, (1982) 149 CLR 431, 474, where Brennan J said:

An equitable interest is not carved out of a legal estate but impressed upon it. It may be convenient to say that DKL R took only the bare legal estate, but that is merely to say elliptically that 29 Macquarie transferred to DKL R the property in respect of which DKL R had declared that it would be a trustee. The charter of 29 Macquarie’s interest was DKL R’s declaration, not the memorandum of transfer; and DKL R’s declaration was moved by the transfer to it of the property to be held on the trust declared.

An equally good metaphor is to see the interest of the beneficiary as being ‘engrafted’ on to the right held by the trustee. This is the language of McLelland J in Re Transphere Pty Ltd (1986) 5 NSWLR 309. Having referred to the judgment of Hope JA in DKL R, he said:

Where a legal owner holds property on trust for another, he has at law all the rights of an absolute owner but the beneficiary has the right to compel him to hold and use those rights which the law gives him in accordance with the obligations which equity has imposed on him by virtue of the existence of the trust. Although this right of the beneficiary constitutes an equitable estate in the property, it is engrafted onto, not carved out of, the legal estate.

We will see later that this undoubted truth is often forgotten by courts and commentators.

2.1.4 What do trusts look like?

It will help enormously if you have an idea of what a typical settlor-created trust looks like. There is no standard form, but two very common examples of trust instruments are set out in Hayton & Mitchell.
ACTIVITY 2.1
Read the two trust precedents in Hayton & Mitchell (Chapter 1: ‘Introduction’ paras 1–160–1–193, in your study pack).

a. Ask yourself what each provision in the precedents is trying to do.

b. Identify the different approaches taken by those drafting the precedents.

c. Does either precedent give enough guidance to the trustee as to how they should administer the trust?

2.2 Equity

You need to know about the system of law called equity. From your study of the English legal system, you may already be familiar with the fact that English law comprises two systems of case law: common law and equity. An understanding of this division is essential to an understanding of trusts, for the trust device is only recognised by equity, not the common law. The rules of equity are those rules which, prior to the passing of the Judicature Acts 1873–75, were administered by the Court of Chancery. Until that time, there were physically separate courts of common law and equity, each applying their own rules. Sometimes those rules were the same, but often they were different. Today there are no separate courts of law and equity and every High Court judge is empowered to administer the law of both jurisdictions. For the sake of convenience, however, many actions which would have formerly been heard in a court of equity are now assigned to the Chancery Division of the High Court of Justice. For more information about the Chancery Division, see: www.justice.gov.uk/courts/rcj-rolls-building/chancery-division

Although the law of trusts is part of the law of equity, equity's jurisdiction is not limited to trusts. You will, for example, have had some contact with equity in your study of the law of contracts. One example is the doctrine of promissory estoppel, through which equity can enforce a gratuitous promise that has been relied upon to the detriment of the promisee. Another example is in the range of responses available for breach of contract. The common law provides only damages, while specific performance and injunctions are available. Though the rules which govern the law of trusts are drawn exclusively from equity, at times some knowledge of particular areas of the common law will be needed, most particularly the rules of common law relating to the transfer of personal and property rights. Those legal rules will, however, be explained as we go along.

2.2.1 Conflicts between law and equity

Given that the rules of law and equity are sometimes different, situations are bound to arise where there is a conflict between the answer given to a dispute at common law and that given in equity. A conflicts rule was therefore needed for such situations, and it was held as long ago as 1616 in the Earl of Oxford's case that where the rules of common law and equity were in conflict, the rules of equity prevail. That is still the law today: Senior Courts Act 1981, s.49. This does not mean that the rules of common law are redundant. As a matter of history, the common law predated equity by many years, and the reason why rules of equity arose was to deal with situations in which the common law was unable to give relief. The rules of equity do not, therefore, comprise a complete system of law. Rather, they presuppose the existence of the common law, acting as a gloss or supplement to it in certain well-defined circumstances. The common law is a complete system and could survive (though not very well) without equity. But, as Maitland in *Equity – A Course of Lectures* (1909) famously explained:

At every point equity presupposed the existence of common law ... Equity without common law would have been a castle in the air, an impossibility.
Fusion

As we have seen, the separate courts of common law and equity were merged in the latter half of the nineteenth century. It has been a controversial question ever since whether that merger was merely one of administration, with the different rules being left intact and only the power to enforce them now being vested in all the judges, or whether there was a merger of substance, with the result that we no longer have separate rules of law and equity but simply rules of law. This is the fusion debate. You must make up your own mind about who in this controversy is right, though the authors of this guide would adopt the view expressed by Ashburner, that ‘the two streams of jurisdiction, though they run in the same channel, run side by side, and do not mingle their waters’. None of us, however, would advocate the continuation of unprincipled differences between law and equity.

The content of equity

Many students make the mistake of thinking that equity is synonymous with fairness or justice, and that the rules of equity are simply what the student (or a judge) thinks is fair or just. This could not be further from the truth. Indeed, were that so, the rules of equity would have no substantive content and would not be a fit subject for study at university level. It is therefore vital to appreciate at an early stage that equity is a system of rules in exactly the same way as the common law, and that it has a system of precedent which is exactly the same as that operated at law. The legal method employed by the equity judges is no different from that employed when they wear their common law hats. Although equity started out as providing ad hoc responses to common law injustices (as indeed did the common law), it soon settled down to become a coherent system of rules, the content of which did not alter with the identity of the particular judge. As long ago as 1818, Lord Eldon, one of the greatest equity lawyers, in one of his last judgments before retirement, responded to such a criticism by saying:

Nothing would inflict on me greater pain in quitting this place than the recollection that I had done anything to justify the reproach that the equity of this court varies like the length of the Chancellor’s foot. (See Gee v Pritchard (1818) 2 Swan 402, 414.)

There has recently been a disturbing trend which says that everything should turn on whether the defendant was acting ‘unconscionably’ in what they have done: see Bank of Credit and Commerce International (Overseas) Ltd v Akindele [2000] EWCA Civ 502, [2001] Ch 437; Pennington v Waine [2002] EWCA Civ 227, [2002] 1 WLR 2075; Pitt v Holt [2013] UKSC 26, [2013] 2 AC 108. Precisely what is ‘unconscionable’ is never defined, and, given that it is just as vague as ‘just’ or ‘equitable’, it must therefore take content from the perception of the individual judge trying the case. ‘Unconscionable’ expresses a conclusion, not a rule we can apply to resolve disputes, and if such an approach takes root, then we risk losing the constitutional principle of the rule of law. For that reason alone, it should be asked whether such a development is to be welcomed.

Equitable maxims

You will from time to time come across a number of equitable maxims. These are very generally stated rules. The use of maxims in law is an ancient one, and the common law knew its fair share. Although no one would nowadays spend time discussing common law maxims, students of trusts are introduced to the equitable maxims. These should, however, be treated with caution, for they are often so widely stated as to be of little practical use. Rules should instead be taken from cases, just as with the common law, which will at least have the merit of ensuring that the particular rules are not then taken out of context.
Activity 2.2


a. What were the facts and decision of the case?

b. What were the judge’s reasons for rejecting the argument that equity was synonymous with ‘fairness’?

2.3 Comparison with other legal concepts

One of the best ways to understand something is to compare it with things which are different but closely related, thereby understanding the differences between them. If, for example, we want to understand what leopards are, we need to know how they differ from jaguars, tigers and the other big cats. So too with trusts. If we are to understand trusts, we need to know how they differ from a number of other similar legal relationships: agency, bailment, contract and debt.

2.3.1 Agency

A trustee is not by virtue of their office an agent of the beneficiary. When entering into contracts as trustee, the trustee alone incurs a liability to perform them. If the trustee were the agent of the beneficiary, the beneficiary too would become liable under the contract. An agent may also be a trustee, though everything will turn on the terms of the contract of agency. Suppose that you are going abroad for a year and appoint an estate agent to let and manage your house. Whether the agent merely owes you the amount of rent received from your tenants or holds it for you on trust depends on whether the agreement between you provided for the creation of a trust. An example of a contract using the trust device is Royal Brunei Airlines v Tan [1995] UKPC 4, [1995] 2 AC 378 (discussed in Chapter 16), where a travel agent was appointed to sell tickets for the plaintiff airline on condition that all monies received by the agent were to be held for the airline on trust.

Reflection point

Why might the use of a trust device make a difference in such cases?

2.3.2 Bailment

Suppose again that you are going abroad for a year. You may have a painting which you do not want to leave in the house. You therefore hand it to a friend to look after during your absence. This will probably amount to a bailment, though it could be a trust. Everything will depend on the location of your title to the painting, which is your right to exclusive possession of it. If you transferred it to your friend, then they would be a trustee of that right for you. If, however, you kept your right yourself, handing over only the possession of the painting temporarily, then the transaction would create a bailment, not a trust. The difference between the two is crucial for several reasons. First, if, in breach of instructions, your friend sold the painting to an innocent buyer, it would matter a great deal whether you created a bailment or a trust, since the buyer would acquire only your friend’s title to the painting. If your friend was a bailee, then the buyer would acquire only a temporary right to possession and you would be able to recover the painting or its value from the buyer (who would be guilty of the tort of conversion, no matter how innocent the buyer may have been). The basic rule is nemo dat non quod habet (no one gives what he does not have), and since your friend did not have your title to the painting, they could not transfer it to the buyer. But if your friend was a trustee, the buyer’s position would be different, since your friend would have the right in question and so would be able to transfer it to third parties. You, of course, would have rights under the trust, but, as we will see in Chapter 4, such rights usually cannot be enforced against an honest buyer.
2.3.3 Contract

There is no clean division between contract and trust, though some judges have attempted to draw one (see e.g. Re Cook’s ST [1965] Ch 902, discussed in Chapter 9). Indeed, there can be no hard and fast line between contract and trust because contract is a source of rights while trust is a way of holding rights. Indeed, many of the rights held in trust are born of contract. A simple example will illustrate. Suppose I open a bank account and pay in £1,000. I have a right born of contract that the bank repay me £1,000 on demand. If I then declare that I hold that right on trust for my children, it is impossible to say that this is now a case of trust and not contract. In truth, it is both.

The other point, of course, is that contract is an essentially consensual institution. Although some of the terms of a contract may be dictated by the law rather than the parties themselves, no one is ever forced to be a contracting party. This is not the case with trusts. Although the vast majority of trusts are settlor-created, some are forced upon unwilling parties.

2.3.4 Debt

The distinction between trust and debt is more difficult. The relationship between trustee and beneficiary is not one of debtor and creditor. In other words, the trustee does not owe the value of the rights they hold to the beneficiaries. Take a simple example. If I lend you £100, your obligation to repay me £100 will not be removed if the cash I gave you is stolen from you. But if you hold £100 on trust for me, then the total loss of the subject-matter of the trust (so long as it was without fault on your part) will mean that it is not possible for me to bring an action against you, claiming that you owe me £100 (see Morley v Morley (1678) 2 Cas Ch 2). It is possible for someone to be both a debtor and a trustee at the same time, with the borrower holding the money in trust for the lender until certain conditions are fulfilled: Barclays Bank Ltd v Quistclose Investments Ltd [1968] UKHL 4, [1970] AC 567; Twinsectra Ltd v Yardley [2002] UKHL 12, [2002] 2 AC 164. Once the condition is fulfilled, the trust ceases to exist and the debt continues. If the condition cannot be fulfilled, then the debtor as trustee must return the money to the lender as beneficiary, thus ending both relationships.

Activity 2.3


a. What were the facts and decision in each case?

b. What would have been the result had trusts not been found?

Activity 2.4

Is it possible to maintain strict divisions between trust and agency, trust and bailment, trust and contract, and trust and debt?

Explain your views.

Self-assessment questions

1. What are trusts and why are they created?

2. What is the relationship between the law of equity and the law of trusts?

3. What similarities are there between common law and equity?

4. What are the differences between the two?

5. What was the effect of the Judicature Acts 1873–75?

6. In a trust, who are (a) the ‘settlor’, (b) the ‘beneficiary’ and (c) the ‘trustee’?
ESSENTIAL READING
At least one of the following:
- Oakley, Chapter 1: ‘Introduction’.
- Pettit, Chapter 1: ‘History of the Court of Chancery and Introduction to Equity’ Section 1–4 and Chapter 2: ‘The Trust Concept’.

FURTHER READING

SAMPLE EXAMINATION QUESTIONS
No sample questions are given here because although the topics covered in this chapter are vital for an understanding of the law of trusts, they are not specifically examinable.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>I can explain in outline what is a trust, and why people create trusts.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can explain the difference between law and equity and the role of equity in the enforcement of trusts.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain how trusts differ from similar concepts.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked 'need to revise first', which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.1 What is a trust?</td>
<td></td>
</tr>
<tr>
<td>2.2 Equity</td>
<td></td>
</tr>
<tr>
<td>2.3 Comparison with other legal concepts</td>
<td></td>
</tr>
</tbody>
</table>
3 Types of trust

Contents

Introduction ......................................................... 18
3.1 Express trusts ........................................ 19
3.2 Discretionary, fixed and bare trusts .............. 19
3.3 The protective trust ................................ 21
3.4 Trusts arising by operation of law ............... 22
3.5 Resulting trusts ......................................... 24
3.6 Testamentary and inter vivos trusts .............. 25
3.7 Purpose trusts: private and public (charitable) purpose trusts 25
Reflect and review .............................................. 28
Introduction

There are several different kinds of trust, and learning what these are is to a large extent learning the meaning of the different terms used to classify trusts. This terminology is historical, and to some extent unsystematic and even contradictory. Nevertheless, grasping the different kinds of trust, and the various terms used to classify them, is vital for two reasons:

1. The first, practical reason is that if you do not get a grip on these terms you will not be able to understand most of what judges and lawyers say when they talk about trusts, and indeed you will have an impossible time understanding the rest of this subject guide.

2. Just as importantly, understanding any area of law turns on being able to see the distinctions it draws and classifications it devises, for this is how it is made comprehensible and coherent, so that justice is done and like cases decided alike.

Do not worry if everything is not entirely clear when you have finished working on this chapter. We will return to all of these issues throughout the guide. The main purpose of this chapter is simply to acquaint you with the language of the subject so that you can work through the other chapters with some measure of comprehension.

Essential reading


Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- indicate where some of these terms may have several, perhaps conflicting, meanings
- outline the structure of the various kinds of trust to which these terms refer and be able to explain the bases upon which they classify trusts
- explain the operation of the protective trust.
3.1 Express trusts

The central case of the trust is the express trust. An express trust is one which is deliberately created by the holder of the rights which will be held in trust. As we will see in Chapter 5, this person is called the ‘settlor’ because they ‘settle’ the rights on trust, either declaring that they will henceforth hold some particular rights on trust for specified persons (the beneficiaries), thus becoming a trustee for them, or by transferring the rights to other persons to hold on trust for the beneficiaries. The reason why such trusts are called express is because a declaration of trust is expressed, (literally ‘pushed out’) in the same way that toothpaste is ‘expressed’ from the tube, by the settlor. Such an expression of intent is known as a declaration of trust. An express trust, therefore, is no different from a declared trust. The essential points to grasp about express trusts are the following:

1. It is not every declaration of trust which will be effective to create a trust. In order for it to have this effect, certain substantive requirements must be satisfied. These requirements will occupy us in Chapter 5. You can think of them in much the same way that you understand the requirements for the successful formation of a contract. To take just one example, just as there must be an intention to create legal relations in the law of contract, so there must be an intention to subject the right-holder to the sanction of the court in the law of trusts. For that reason, we will see that ‘precatory’ words, words expressing merely a hope or desire that a right-holder will act in a particular way, are not normally sufficient to bring a trust into being.

2. The power of a right-holder to create a trust reflects a principle of ‘freedom of trust’ similar to the succession law principle of ‘freedom of testamentary disposition’ and the contractual principle of ‘freedom of contract’. Settlors can, within the limits of the law, divide up the entitlements under the trust in any way they choose, providing different kinds of interests for different beneficiaries or different charitable purposes.

3.2 Discretionary, fixed and bare trusts

3.2.1 Discretionary and fixed trusts

A settlor may decide to divide up the interests of the beneficiaries according to a fixed plan but very often may decide to take a ‘wait and see’ approach, leaving the actual shares or interests that the beneficiaries will receive to be decided later. For example, the settlors may want to create a trust for their children, but leave it open how much each child will receive, so as to take account in later years of their differing circumstances.

1. A fixed trust is one in which the interests of the different beneficiaries are determined at the outset and the trustees have no decisions to make as to how they should distribute the trust rights.

2. A discretionary trust is one in which the trustees have such a dispositive discretion (i.e. a discretion as to how to dispose of the trust rights).

Discretions may be shaped in various ways, but the typical case is one in which there is a class of persons to whom the trustees may distribute the trust funds in such shares as they, in their discretion, decide. Thus they can choose to distribute the rights evenly or in unequal shares by giving some to all or only to one or a few of those in the class.

The fixed or discretionary nature of a trust turns upon whether the trustees have a discretion in their distribution of the trust rights. Being fixed does not mean that the actual amount that a beneficiary will receive is determinable from the outset. For example, in a trust of company shares where the income of the shares (the dividends) go to Paul as long as he lives and then the capital (the shares themselves) to Peter, it is impossible to tell how much Paul will get at the outset, for that will depend on the value of the dividends on the shares over time and how long Paul will live.
Nevertheless, the trust is still fixed because the trustees have no choice but to transfer that income to Paul.

Furthermore, a beneficiary may receive a contingent or defeasible interest under a trust. A contingent interest is one which will only arise if a certain event occurs. So, for example, a trust might provide that your daughter, Samantha, is to receive an income interest, but only if she completes her law degree successfully. A defeasible interest is one which may come to an end upon the happening of a certain event. You might give Samantha an interest in income, which will terminate if she wins £1 million or more in a lottery. Though under both these kinds of interests, it is not certain at the outset what, if anything, Samantha will take under the trust, they are still classified as fixed because the trustees have no dispositive discretion.

A trust can include both discretionary and fixed elements. For example, you may settle a trust of company shares, with the income of the shares to be distributed as it arises among your children, Tom, Dick and Mary, in such shares as your trustees, in their discretion, decide, and with the capital (the shares themselves) to be distributed in equal shares to Tom, Dick and Mary once the youngest turns 18 years of age. The distribution of income is discretionary, but the capital interests are fixed.

### 3.2.2 Bare trusts

A bare trust is one in which the terms of the trust are minimal. Under a bare trust, the trustees hold the trust rights 'to the order' of the beneficiaries, which means that the trustees simply hold the rights and do the bidding of the beneficiaries. In this respect, a bare trust is just the most minimal kind of fixed trust, under which trustees have no discretion. A distinction is sometimes drawn between simple (bare) trusts and 'special' trusts (with more or less complicated terms, fixed or discretionary). Why might someone set up a bare trust? In various circumstances, a bare trust can be very convenient. For example, you might transfer company shares to your broker to hold on bare trust for yourself. The broker will be able to engage in all the legal procedures to deal with the trust rights, so you do not have to attend to that, and the broker will just follow your instructions about the various transactions, which you might find convenient to give over the telephone, for example. For this reason, trustees under bare trusts are sometimes called 'nominees', to indicate that they hold the rights in name only directly for another (the beneficiary). Such trusts are sometimes called 'nomineeships'.

The terminology of fixed trusts and discretionary trusts classifies trusts by a criterion of dispositive control by the trustee. In a fixed trust, the trustees have no choice as to how to distribute the trust rights, but no one else has any say, and it is the trustees’ duty to ensure that the correct distribution takes place. In a discretionary trust, the trustees themselves have the power of choice over the distribution of the trust rights.

All trusts which arise by operation of law are bare trusts.

**ACTIVITY 3.1**

Make a short spoken presentation explaining the difference between fixed and discretionary trusts, giving practical examples.

No feedback provided.

**Summary**

An express trust is one which arises in response to an effective manifestation of intention on the part of a right-holder that a trust should arise. This manifestation of intention is known as a declaration of trust. Express trusts are therefore declared trusts. The simplest form of declared trust is the bare trust or nomineeship, under which the trustee holds rights to the order of the beneficiary. However, interests under trusts are commonly structured by the use of contingent interests (which may arise or lapse on the occurring of events) and by providing the trustee with dispositive discretions (to allocate trust rights among a class of persons). Trust provisions
which incorporate dispositive discretions are termed ‘discretionary’, and those not incorporating such discretions are called ‘fixed’. All trusts arising by operation of law are bare trusts.

**Activity 3.2**

You have just won £1 million in a lottery and decide to settle half of the money on your loved ones. Devise a trust, deciding how you wish to divide up the money among them, incorporating both fixed and discretionary elements, and if you wish, contingent and defeasible interests.

### 3.3 The protective trust

**Essential Reading**
- Trustee Act 1925, s.33.
- Cases: *Re Burroughs-Fowler* [1916] 2 Ch 251; *Re Baring’s Settlement Trusts* [1940] Ch 737; *Re Coleman* (1888) 39 Ch D 442; *Re Gourju’s Will Trusts* [1943] Ch 24; *Re Westby’s Settlement* [1950] Ch 296.

At least one of the following:
- Martin, Chapter 7: ‘Protective trusts’.
- Oakley, Chapter 8: ‘Protective trusts’.
- Pettit, Chapter 4: ‘Classification and juristic nature of trusts’, Section 2 ‘Discretionary and protective trusts’.

**Further Reading**

A beneficiary under a fixed trust has an interest which can be transferred (assigned) to others. So, for example, if you are a beneficiary of a trust who is entitled to receive the income earned by the trust rights each month (i.e. an ‘income’ beneficiary) you can assign that entitlement to, for example, your spouse and, if you do so, your spouse will then have the right to demand the income payments each month from the trustee. That interest, assuming it has not been assigned, will form part of your estate if you become insolvent. Thus the trustee will have to pay that income to your trustee in bankruptcy, who is the person who takes over certain rights in your estate and will use that income, along with all the rest of your rights, to pay off your creditors.

To prevent interests under a trust from being assigned by beneficiaries or being used to pay their creditors should they go bankrupt, the settlor might use the device of a **protective trust**. Such a trust normally utilises the device of a certain kind of defeasible interest (see Section 3.2.1), which is a determinable life interest followed by a discretionary trust. The trust will commonly confer a life interest upon the principal beneficiary which will terminate upon their bankruptcy or any other event whereby the beneficiary would lose the right to retain the income from the trust (e.g. assignment of the interest). If such an event occurs, the trustees will automatically hold the rights on a different trust, usually a discretionary trust in favour of the principal beneficiary and their family. Once this happens, neither the principal beneficiary nor their creditors or trustees in bankruptcy will have any entitlement to the trust rights since the principal beneficiary will then have only a hope of receiving some income if the trustees exercise their discretion in the principal beneficiary’s favour. This is only a mere hope (in Latin, a *spes*) which cannot be assigned or otherwise transferred.

The main points to note regarding protective trusts are as follows:

- They may be created by the inclusion of appropriate terms in a trust instrument (in which case regard must be had to the particular words used, especially as to the formulation of the determining events) or simply by incorporating the statutory protective trust, set out in s.33 of the Trustee Act 1925.
An attempt by a settlor to create a protective trust in their own favour is not void per se, but will not protect the settlor's rights under the trust where the first determining event to occur is the settlor's bankruptcy: *Re Burroughs-Fowler*.

Decisions as to whether a determining event has occurred in a particular case must be read in the light of the definition of the determining event being considered. For example, the express clause in *Re Hall* was narrower than the statutory term construed in *Re Gourju’s Will Trust*, thus justifying different decisions on similar facts. The s.33(1)(i) formulation of the determining event is very wide:

> Upon trust for the principal beneficiary during the trust period or until he ... does or attempts to do or suffers any act or thing, or until any event happens, other than an advance under any statutory or express power, whereby, if the said income were payable during the trust period to the principal beneficiary absolutely during that period, he would be deprived of the right to receive the same or any part thereof....

The statutory language is difficult, but if you concentrate on the passages in bold first, it is clear that the first fixed trust for the primary beneficiary will end if anything happens, whether by the beneficiary's own act (e.g. an assignment) or not (e.g. a creditor petitioning the court to declare the beneficiary bankrupt). That will result in the beneficiary losing the right to be paid by the trustee.

**Summary**

A protective trust is a defeasible fixed trust (the primary trust), which on the occurrence of a defeating condition, is replaced by a discretionary trust (the secondary trust). By broadly framing the defeating conditions to include any event whereby the beneficiary of the primary trust (the primary beneficiary) loses their fixed interest in that trust, the trust funds are prevented from going to the primary beneficiary's creditors. Thus the trust is protected in the case of the beneficiary's insolvency.

### 3.4 Trusts arising by operation of law

#### 3.4.1 How rights arise

Although the manifestations of consent underlying contracts, wills, deeds, and declarations of trust are a common source of legal rights, rights can arise in other ways. In private law, rights can also arise by the commission of a wrong (tort), by unjust enrichment, and by miscellaneous other events. One question for the law of trusts is when these events trigger trusts and not merely a personal right to a money payment, injunction, or other remedy.

#### 3.4.2 Statutory trusts

There are a number of situations in which the legislature has thought it convenient to use the trust device as a cure for certain problems. In such cases, the trust is a creature of statute. You may have already come across some of these in land law. Thus, if I attempt to convey a title to land to Fred and Joe as tenants in common, statute provides that the effect of my action is to convey the title to Fred and Joe as joint tenants on trust for themselves as tenants in common: s.34(2) Law of Property Act (LPA) 1925. In this course we are not concerned with statutory trusts, for they are used by the legislature on an ad hoc basis and only make sense when examined in context.

#### 3.4.3 Constructive trusts

The term 'constructive' is ambiguous, but in the context of trusts, it means a trust which is literally 'constructed' by the court rather than by an individual right-holder through a declaration of trust. We came across examples of constructive trusts in the last chapter in *Chase Manhattan v Israel-British Bank* and *FHR European Ventures LLP v Cedar Capital Partners LLC*. The vital fact to realise about both these cases is that
the trust arose even though there was no declaration of trust by the right-holder concerned. Constructive trusts, therefore, are ‘not-declared’ trusts. But to say that they arise for reasons not involving a declaration of trust is not particularly helpful, for it gives only a negative description, telling us why the trust does not arise rather than why it does. It is one of the tasks of judges and commentators working in the area of trusts to come up with a typology of constructive trusts so that this question can be answered. The best attempt so far is that of the late Professor Birks, who said that all private law rights owe their origin to one of four events: manifestations of consent, wrongdoing (breaches of duty), unjust enrichment and other events. As those trusts which arise as a response to manifestations of consent are express trusts, that leaves constructive trusts to occupy the last three heads. And there is no doubt that each head has content. Thus, the trust in *FHR European Ventures LLP v Cedar Capital Partners LLC* can be seen as a response to the commission by the agent of the wrong of breach of fiduciary duty, and in *Chase Manhattan* it arose as a response to the unjust enrichment of the defendant caused by its receipt of the mistakenly paid US$2 million. As for the miscellaneous other events, by far the majority of constructive trusts fall within it. So, for example, a contract to sell an estate in land turns the seller into a trustee of that estate for the purchaser, even though there is no declaration of trust, no wrongdoing, and no unjust enrichment. The crucial questions in all cases of constructive trusts are why the trusts arose and whether they should.

Constructive trusts can be sub-divided into ‘institutional’ and ‘remedial’ trusts. Unfortunately, these terms do little to explain the idea behind them. It might be seen as a rule of law and the rule of man, the man (or woman) in question being the individual judge. Thus, institutional constructive trusts arise because of the application of legal rules, albeit rules developed incrementally by courts, whereas remedial constructive trusts arise because an individual judge thinks it is fair that it should, despite the fact that the rules developed by the courts say that on the particular facts there should be no trust. It is a nice question whether English law has remedial constructive trusts. Given our legal system’s commitment to the rule of law, it is hoped that it does not.

**Constructive trusts of the family home**

Another case of a constructive trust is one with which you may be familiar from studying property law. This is the constructive trust of the family home which are cases in which the family home is held in trust for a cohabiting couple even though no express trust was declared. The House of Lords and Supreme Court have dealt with this trust in *Stack v Dowden* [2007] UKHL 17, [2007] 2 AC 432 and *Jones v Kernott* [2011] UKSC 53, [2012] 1 AC 776, but without explaining exactly why the trust arises.

### 3.4.4 Implied trusts

There is an uncertain and probably moribund category of trusts called implied trusts. In law, ‘implied’ can mean at least two different things: (1) implied by law (i.e. imposed by law), or (2) implied in fact (i.e. inferred from the facts). So, for example, the law for many years said that the reason why people had to repay mistaken payments was that they had impliedly promised to do so. But when the defendant in *Moses v Macfarlan* (1760) 2 Burr 1005, 97 ER 676 proved by evidence that he had made no such promise, the court said that it did not matter because the promise was implied by law (i.e. ‘imposed’ by law). Implied in fact, on the other hand, means an inference of the parties’ intentions drawn from what they said and did. Thus, when in the morning I take my car to the garage for repair, there is promise implied in fact on my part to pay for those repairs when I pick it up later that evening, even though I said nothing of the sort. Whatever ‘implied’ means in the law of trusts, we can immediately see that it is a redundant category. If it means a trust implied in law, then it is no different from a constructive trust. If it means a trust implied in fact, then it is no different from an express trust. Because of the ambiguity inherent in the words ‘implied trust’, the term should be avoided, and in that regard it is notable that it is rarely used today.
Summary

Some trusts arise by operation of law, that is, for reasons other than an effective declaration of trust. In other words, the trust arises as an equitable response to certain factual circumstances. What is often lacking is a coherent explanation of why this is done.

3.5 Resulting trusts

In this context resulting comes from the Latin resalire, meaning ‘to jump back’. A resulting trust can arise in favour of a person who causes rights to be transferred to another to compel the recipient to hold those rights in favour of the person who caused the transfer. When this occurs, we call it a resulting trust. Thus, any situation in which A conveys transfers rights to B which B, for whatever reason, then holds on trust for A is a resulting trust. The immediate problem, however, is that the term ‘resulting’ provides no clue as to why that trust arose. It may have done so because A told B to hold the rights for him on trust, as in the nomineeship example discussed above. Therefore, it may be an express trust. Or it may have arisen, as in Chase Manhattan, because A’s transfer was mistaken (i.e. a constructive trust). For this reason, resulting trusts overlap with express and constructive trusts, and should not appear in the same series. Unfortunately, the dominant classification of trusts in English law makes them so appear.

One way to make some sense of resulting trusts is to add another word to indicate why they arise. This was the strategy of Megarry J in Re Vandervell (No 2) [1974] Ch 269, who added the labels ‘presumed’ and ‘automatic’. In his view:

- A ‘presumed’ resulting trust generally arises where A transfers a right to B gratuitously (i.e. taking no payment of any kind in return, ‘for no consideration’ or ‘voluntarily’) and there is no evidence of why A did so. Likewise, if A pays C to convey a right to B then, in the absence of evidence of the manifested intentions of A and provided certain other conditions are met, B will hold the right on ‘resulting’ trust for A.

- An ‘automatic’ resulting trust arises when a transfer is made on trusts which are either wholly or partially void. Thus, if A conveys a right to B to hold on trust for C for life, but says nothing about how B is to hold it after C’s death, the trust ‘fails’ so far as the remainder is concerned, and B will hold the right on ‘resulting’ trust for A.

There are two questions to be asked about resulting trusts. First, what is the fact proved by presumption in the presumed resulting trust which causes the courts to say that there is a trust? One theory is that the presumed fact is a declaration of trust by the transferor for themself. As such, it is a form of express trust. As we will see in Chapter 12, this is controversial, and some argue that the fact presumed triggers a trust that arises by operation of law, in other words, a constructive trust. Second, why does the ‘automatic’ resulting trust arise? Is it because the court ‘presumes’ an intention on the part of the transferor that it should, or is it because the courts impose a trust? And if the latter, why do the courts impose such a trust? If it is indeed a trust which is imposed by the courts, then it too is nothing more than a constructive trust. On either view, resulting trust would appear to be a redundant category.

Summary

A resulting trust arises in favour of someone who caused the rights in question to be transferred to the resulting trustee. Since Re Vandervell (No 2), two kinds of resulting trust have been recognised. Presumed resulting trusts arise because of an evidential presumption which arises on proof by evidence of certain primary facts. If the presumed fact is a declaration of trust, presumed resulting trusts are a species of express trust, and if not, they must be constructive. Automatic resulting trusts arise when a transfer of rights is made pursuant to a declaration of trust which is in some sense defective or incomplete. The question then is why a trust should arise in such circumstances. If it is not because of a presumption of intention, then they are certainly constructive. Either way, the category of resulting trust would appear to be redundant.
3.6 Testamentary and *inter vivos* trusts

A testamentary trust is an express trust which is set out in a person’s will, and comes into operation when the testator dies and their will is executed by their executors. Typically the executors are also the first trustees of any trust which arises under someone’s will. By contrast, an *inter vivos* (‘among the living’) trust is one which is created by the settlor when alive.

**Self-assessment questions**

1. Define:
   a. an express trust
   b. a discretionary trust
   c. an automatic resulting trust
   d. a constructive trust
   e. an implied trust
   f. an *inter vivos* trust.

2. What is ‘fixed’ in a fixed trust?

3.7 Purpose trusts: private and public (charitable) purpose trusts

Every express trust exists for a purpose in the sense that a settlor creates it with some purpose in mind. The same is true of constructive trusts which arise by operation of law to fulfil the purpose for which that legal rule was created. As we have seen, the central case of the express trust is one in which rights are transferred to trustees on terms which give the beneficiaries rights against the trustees to the payment of income or capital, usually over a period of some years. A purpose trust, properly so called, is one in which no beneficiaries have rights to income or capital but which is devoted to the carrying out of some purpose, for example, to devise a 40-letter alphabet for the English language (*Re Shaw* [1957] 1 WLR 729). While it might be true that a great many individuals could in fact benefit from such a trust, they are not beneficiaries in the way that beneficiaries of a normal trust are. They do not have any defined interests in the trust (such as capital, income or defeasible interest) nor can they enforce the trust against the trustee. Therefore, trusts for non-charitable purpose are usually void. If a settlor tries to create a purpose trust, the trust will fail at the outset.

There is, however, a very important exception to this principle. A trust for charitable purposes, such as a trust to assist the poor, will be valid. How, you might ask, is such a trust enforced? Can the poor compel the trustee to use the rights as intended? No. The Charity Commission for England and Wales has the power to enforce such trusts on behalf of the Crown: Charities Act 2011, ss.13–15. It is for this reason that charitable trusts are also known as ‘public trusts’, because they involve the participation of the state. By way of contrast, purpose trusts which are not accepted by the law as charitable are often called ‘private purpose trusts’.

As we have seen, the basic rule is that private purpose trusts are void. There is, however, a tiny class of exceptions, all of which are testamentary trusts. These are trusts for the provision and upkeep of graves and monuments, the care of the testator’s animals or for private masses for the better repose of the testator’s soul. The enforcement mechanism is peculiar and fragile, as we shall see in Chapter 11. As we shall also see in Chapter 11, certain recent cases may appear to have made inroads into the rule against private purpose trusts.
Summary

Purpose trusts are those in which funds are devoted to the carrying out of a purpose rather than conferring rights on beneficiaries. Such trusts have no beneficiaries, and for this reason, among others, most private purpose trusts are invalid. Charitable or public purpose trusts are valid and are enforced against the trustees by the Charity Commission.

Essential reading
At least one of the following:

- Oakley, Chapter 2: ‘The classification of trusts’.
- Pettit, Chapter 4: ‘Classification and juristic nature of trusts’.

Further reading

Activity 3.3


a. Under her will, A provided £1 million to be held on trust, the income to be distributed for a period of 21 years to her children and grandchildren in such shares as her trustees shall in their absolute discretion decide, though any child or grandchild will lose any further possibility of receiving money if they establish a residence outside the UK. At the end of the 21-year period, the capital is to be divided evenly between the National Trust and the Red Cross.

b. A house was purchased in the name of a husband with 20 per cent of the money provided by the husband’s parents as a wedding gift and the remaining 80 per cent by a bank loan to the husband secured by a mortgage over the title to the house. The Court of Appeal decided that his wife was entitled to a 50 per cent share in the house, first because the wedding gift was money given to both her and her husband, and second, because the parties took a ‘share and share alike’ attitude to their possessions while married. (See Midland Bank v Cooke [1995] 4 All ER 562.)

c. Fred transferred £50,000 to trustees on trust to build a ‘useful memorial to myself’. (See Re Endacott [1960] Ch 232.)

d. Arthur transferred £10,000 to trustees on trust for ‘such objects as I shall declare in writing’. Arthur died before declaring any such objects.

e. Beatrice transferred 100 of her shares in Super plc to her infant niece Florence and later died. There is no evidence that she spoke to anyone about the transfer. (See Re Vinogradoff [1935] WN 68.)

f. In compliance with their contract to pursue the purchase land for commercial development, Fred and Bill each transferred £100,000 to a solicitor to complete the purchase. The solicitor wrongfully paid £10,000 of this to his nephew as a birthday present.

Sample examination questions

Question 1 How does the law classify trusts? Are there any ambiguities and inconsistencies in the classifications?

Question 2 Under a trust created 10 years ago, investments worth £1 million are held by trustees upon trust to pay the income to Albert for life upon protective
trusts with remainder (i.e. after his death) to such of Albert’s children as Albert by deed or will shall appoint and in default of appointment in trust for such of his children as attain the age of 18 and if more than one in equal shares absolutely.
Albert is married and has three children, Betty, Clare, and Donald, aged 23, 21, and 2 respectively.

Advise the trustees: (a) as to their duties in relation to the application of trust income in the event of Albert’s bankruptcy; (b) as to the distribution of the capital of the trust fund in the event of Albert’s death in the near future.

ADVICE ON ANSWERING THE QUESTIONS

Question 1 This is a wide-ranging topic which can be addressed in different ways. However, the two different parts should each receive sustained attention. The law classifies trusts in different cross-cutting ways for different purposes. The distinction between fixed and discretionary trusts is based on the structure of the trust (i.e. the terms of the trust which determine how the rights are to be distributed). It distinguishes cases where the trustee has no dispositive discretion (i.e. where the trustee merely takes orders as in a bare trust), or where the trust instrument dictates the distribution, from cases where the trustee has significant control by way of his discretion over distribution. The distinction between express and constructive trusts focuses on how trusts arise. Express trusts arise because right-holders intentionally create them, conferring powers and imposing duties on trustees, and giving rights to beneficiaries. Constructive trusts, by contrast, are imposed on right-holders by operation of law. The category of implied trust is probably redundant. Purpose trusts are distinguished from typical trusts for beneficiaries, and the public/private distinction with respect to purpose trusts indicates the mechanism of enforcement and the charitable, public-serving substance of the former. The distinction between testamentary and inter vivos trusts is straightforward, reflecting the way in which a different area of law (the law of succession) interacts with the law of trusts. The special identification of resulting trusts, though a traditional classification, is problematic, given both that it covers two cases of trust arising for seemingly different reasons, and because the term can refer broadly to cover cases outside these two.

The second point to be addressed focuses on the problems of the classifications the law has traditionally adopted. Implied trusts and resulting trusts should be discussed, implied trusts as a classic example of an ambiguous term, and resulting trusts for the uncertain scope of the term, and the difficulty of finding a unifying feature of the two cases of trust typically referred to by the term. The category of constructive trusts, has also historically been used to group particular sorts of trust together which have a wide range of rationales and bases. An answer with respect to constructive and resulting trusts will be enriched by the study of these trusts in depth in later chapters.

Question 2

a. The question does not specify whether the protective trust is statutory or specified in the trust terms. The discretionary trust following the life income would be for Albert, his spouse, and his children under s.33(1)(b)(a) of the Trustee Act 1925 if the trust is statutory, but it may be for a larger or narrower class under specific trust terms. Reference should be made to s.33(1)(c) to show the broad scope for making payments under the discretionary trust, and again, it should be considered that a bespoke provision in a trust instrument might differ. Reference should be made to Re Ashby, Re Coleman and Re Smith in consideration of how Albert himself may be benefited under the discretionary trust.

b. This question concerns the operation of the condition precedent upon each child’s taking a share of the capital: Betty and Clare have attained the age of 18, but Donald has not. Betty and Clare are therefore entitled to a one-third share immediately, while Donald’s must be held for him in trust. (A richer consideration of Donald’s situation will be possible once you have considered the trustees’ powers of maintenance and advancement in Section 4.2.2.) If Donald dies before reaching 18, Betty and Clare will share the remaining capital equally.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


- I can indicate where some of these terms may have several, perhaps conflicting, meanings.

- I can outline the structure of the various kinds of trust to which these terms refer and am able to explain the bases upon which they classify trusts.

- I can explain the operation of the protective trust.

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- 3.1 Express trusts
- 3.2 Discretionary, fixed, and bare trusts
- 3.3 The protective trust
- 3.4 Trusts arising by operation of law
- 3.5 Resulting trusts
- 3.6 Testamentary and *inter vivos* trusts
- 3.7 Purpose trusts: private and public (charitable) purpose trusts
4 The express trust relationship
Introduction

This is the widest-ranging chapter in this subject guide, for it covers a number of essential aspects of the express trust. It is best to look at them together, because they are so closely related. We will begin by examining the way in which express trusts are a legal device generating both personal and proprietary rights. We will then focus on the powers and duties of the trustee and others under the trust, and consider in some detail the trustees’ powers of maintenance and advancement, duty of investment, and power of delegation. We will then focus on the rights of the objects of the trust, in particular the beneficiaries’ rights to information and to collapse the trust under the rule in *Saunders v Vautier* (1841) 4 Beav 115, 49 ER 282.

Essential reading

- Penner, Chapter 2: ‘Property, obligations, and trusts’.

Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- describe the structure of the typical express trust by setting out the rights the beneficiaries have, and the powers and duties that the trustees, and others, may have
- explain in outline the beneficiaries’ rights to follow and trace rights held on trust that have been transferred in breach of trust and the significance of the term ‘equity’s darling’
- set out the typical sorts of administrative and dispositive powers and duties a trustee will have
- describe in detail the law governing the powers of maintenance and advancement, the duty of investment, and the power of delegation
- explain the rights of objects to information and to collapse the trust under the rule in *Saunders v Vautier*. 
4.1 Introduction to rights and duties

The trust is a combination of personal and property rights and duties. What is the difference between a personal right and property right? The basic distinction is that a personal right is a right enforceable against a particular person alone (e.g. a right to the performance of a contract). If I contract with you that you will paint my house, I cannot sue your brother or sister simply because you breach your promise. The only person liable to perform is you. By contrast, a property right is one in respect of a thing which can be enforced against any number of people so long as that thing itself is still in existence. For example, you have a right to exclusive possession forever of this subject guide, a right which the common law compendiously calls ‘title’ (from entitlement). Though that right was transferred to you by the University of London, it binds strangers to that relation. It is a property right and can therefore be enforced against anyone into whose hands the guide may come without your consent.

Under the trust, the trustee owes a number of personal obligations to the beneficiaries, such as the:

- duty to keep the trust accounts (i.e. proper records of the trustees’ dealings with the trust)
- duty to distribute the assets according to the trust’s terms
- duty to invest the trust funds.

If the trustees breach any of these duties they will be personally liable for breach of trust, and the beneficiaries can sue them for a money judgment. But equity also holds that the beneficiaries have rights in respect of the trust rights themselves. They do not, however, have a direct right to possession of the thing which is held in trust. So, for example, if this subject guide were being held for you on trust, it is the trustees, not you, who have the title (i.e. the right to exclusive possession forever). Similarly, if company shares are held in trust for you, it is the trustees who will have the rights to receive dividends and vote at shareholder meetings. They must, however, exercise those rights in the interests of you, the beneficiary, not themselves, and you have a right to call them to account for their exercise of the rights they hold on your behalf.

Most of the beneficiaries’ rights are enforceable only against the trustees. However, there are some rights that can be enforced against strangers to the trust relationship. These arise when the rights are transferred by the trustee in breach of trust to someone who is not a bona fide purchaser (see Section 4.1.1 below). These rights apply equally to express, constructive and resulting trusts. Although third-party recipients will not be subject to the normal duties of trustees (e.g. to invest), and neither will they have the dispositive powers of trustees, they will be obliged to return the trust rights at the beneficiaries’ request. The same rule applies where a sole trustee dies and the rights devolve via their estate. The recipient under their will is likewise under a duty to return the rights at the behest of the beneficiaries. Similar thinking explains what happens when trustees become bankrupt. In such a case, the rights held on trust do not vest in their trustees in bankruptcy, as do almost all their other rights, with the result that the trust rights will not be available to satisfy their creditors’ claims against them. It will be recalled that it was for this reason that the claimant bank in Chase Manhattan was arguing for a trust.

4.1.1 Bona fide purchasers

In the case of property rights, the law has different rules for different kinds of rights when it comes to the enforcement of those rights against other members of society. In the case of goods, for instance this subject guide, the right is very robust. You can in general enforce your right to exclusive possession (your ‘title’) against anyone into whose hands the thing comes, including an innocent person who paid good money for it to someone who stole it from you. There are some limited exceptions to that rule, but the dominant approach is to say that the buyer acquires only the thief’s defective title, which the thief obtained by taking possession, and that your better title was not destroyed by that sale. The innocent buyer bought a title which was not as good as
yours. The Latin expression for this rule is nemo dat quod non habet (no one gives what he does not have).

The protection of rights under trusts is not as strong. The beneficiaries’ rights to recover the trust rights can be enforced:

- against a donee or volunteer (i.e. a person to whom the trustee conveys the trust rights as a gift)
- against the trustee’s trustee in bankruptcy, in whom, as we have seen, the right does not vest
- against the trustee’s personal representative on death

but not against the innocent purchaser for value of the trustee’s legal rights. The effect of such a sale is to destroy the beneficiaries’ right to a reconveyance of the rights, with the result that the transferee takes those free of the trust. The beneficiaries will have personal claims against the trustees for conveying the rights away in breach of trust, but this may be worthless if the trustees are insolvent. The beneficiaries will also have a property right to any proceeds of sale received by the trustees.

More precisely, the trust cannot be enforced against someone who acquires the trust rights as a bona fide purchaser for value without notice. This is usually called the defence of bona fide purchase, which consists of four separate elements that must be satisfied:

- bona fide: the recipient acted in good faith
- purchaser: the recipient acquired legal title and not merely an equitable interest
- for value: the recipient gave good ‘consideration’ (i.e. money or money’s worth) in exchange for the title
- without notice: the recipient did not have notice that the asset was transferred in breach of trust.

The question of good faith will normally be satisfied by showing lack of notice, but it is possible for a person to act in bad faith even without notice of the breach (e.g. if the purchase was part of an illegal transaction).

It may seem like the requirements of purchase and for value are one and the same, but purchase is an old term for the acquisition of legal title other than by inheritance. A person who obtains only an equitable interest is not a purchaser and therefore not entitled to the defence even if they gave full value in good faith without notice. This is because someone else (usually, the trustee) has legal title subject to two competing equitable claims. The beneficiaries’ interest arose first and will almost always prevail over subsequently acquired equitable interests.

Most cases concerning the bona fide purchase defence turn on the question whether the recipient had notice of the breach of trust at the time title was acquired. Therefore, the defence is sometimes called the ‘doctrine of notice’, but this can be misleading since notice is irrelevant if any other element of the defence is not met. Notice may be actual or constructive, and it may be imputed:

- Actual notice: the recipient had knowledge of the breach or was at least alerted to the possibility of breach.
- Constructive notice: the recipient is treated as if they had actual notice. This occurs when the recipient would have discovered the breach if the usual investigations had been made. A purchaser normally makes extensive searches (through a solicitor) when buying land or other expensive assets, and if those searches would have revealed the existence of the trust and possibility of breach, the purchaser will have constructive notice even if they honestly did not have any actual notice. It is sometimes said that such a purchaser is negligent for failing to search, but this is misleading because the purchaser does not owe a duty of care to anyone else when making the purchase and does nothing wrong by failing to search. Everyone is free to take that risk unless acting on someone else’s behalf.
Imputed notice: when the recipient employs an agent (such as a solicitor) to help with the transaction, the agent's (actual or constructive) notice will be imputed to the recipient, even if the agent failed to inform the recipient.

In some cases, the bona fide purchase defence does not extinguish the beneficiaries’ right to the trust asset, but gives the purchaser priority over that right. The defence applies not just to transfers of legal title, but also to grants of other legal rights, such as a legal mortgage or legal lease of land. If the bona fide purchase defence applies, the land will still be held in trust for the beneficiaries, but subject to that mortgage or lease.

4.1.2 Following and tracing trust rights

When the beneficiaries enforce their trust rights against third parties, they are said to ‘follow’ those rights. However, the beneficiaries may acquire substitute rights by operation of law. If, for example, company shares were transferred in breach of trust to a donee, who then sold them to a bona fide purchaser for £1,000, the beneficiaries’ right to the shares would be extinguished. However, the beneficiaries would acquire the right to elect to treat the £1,000 received in exchange as subject to a trust, and then ask for that money to be conveyed to the persons appointed as trustees to receive it. This process is known as ‘tracing’, and it can be used multiple times whenever the trust assets are exchanged for something else. Returning to our example, if the £1,000 received in exchange for the shares were then used to purchase a car, the beneficiaries could elect to treat it as a trust asset. This ability to trace will be lost only when the thing over which the right exists is destroyed (for example, the car is destroyed by fire and there are no insurance proceeds) or there is no exchange product (for example, trust money is spent on a round-the-world cruise). The rules of tracing will be discussed in detail in Chapter 19.

4.1.3 Personal remedies for breach of trust against third parties

In cases of breach of trust, the beneficiaries will also have personal rights against the errant trustees. They can be sued personally to make good losses to the trust which have occurred because of their breach, and unless there is an exemption clause in the trust instrument on which they can rely (see Chapter 16) a trustee is strictly personally liable for breach of trust, in the same way that a contracting party is strictly personally liable for breaches of contract. Moreover, recipients of trust rights, at least those with knowledge that the dissipation was in breach of trust may be also personally liable to restore the value of what they received to the trust, and third parties who dishonestly assist the trustee in a breach of trust will also be personally liable to make good the loss. The liability of these third parties is also discussed in Chapter 16.

Activity 4.1


Explain how the configuration of personal rights and proprietary rights under a trust differs from those in the case of:

a. a bailment
b. an agency under which P’s agent collects rent for him without holding the money he collects on trust
c. a debt.

4.2 Powers and duties of trustees and others

The structure of express trusts can be complicated. In Chapter 3, we saw how an express trust can incorporate different elements, some fixed, some discretionary and some contingent. There we dealt only with dispositive duties and discretions, because the character of distributive duties under a trust has been regarded as an important
basis upon which to classify trusts. Here we elaborate on the structure of trusts, taking trustees’ powers into account. Furthermore, we must notice that it is possible and common for people other than the trustee to have powers or duties under the terms of the trust. To take a typical example, the settlor of a trust may give himself a power to revoke it, so that the trust rights then come back to him.

As we have already seen, ‘dispositive’ powers and duties are those that concern the distribution of trust rights to beneficiaries. ‘Administrative’ powers and duties concern dealings with the trust rights without their distribution, such as investing the trust rights, insuring them or using them to pay fees to solicitors and accountants.

Trustees’ duties and powers are the paradigm of fiduciary duties and powers. ‘Fiduciary’ refers to those duties and powers which a person must exercise in the best interests of another, not himself. A fiduciary must avoid conflicts of interest. Thus, the trustees’ duties must be discharged and their powers exercised only with the interests of the beneficiaries in mind, and in particular, not so as to serve their own interests or the interests of non-beneficiaries such as their own friends and relations who they might otherwise be prone to favour.

A power which is not fiduciary is, in the context of trusts, called a ‘personal’ power, which means that the holder can exercise it, within its proper limits, with their own interests in mind. Fiduciary duties are always held in relation to some person(s), called the principal(s) – it is the principal’s best interests which should govern the power’s exercise. It is very rare for a trustee to hold any personal powers under a trust, for trustees are typically only appointed to carry out the trust for the benefit of the beneficiaries alone; but it is not uncommon for the powers of others under a trust to be personal. For example the commonplace settlor’s power of revocation, mentioned above, may well be personal. The settlor can revoke the trust and obtain a retransfer of the rights because it is in their own interests so to do. Indeed, it might be odd to think that the settlor would hold such a power as a fiduciary to the beneficiaries, for in what circumstances would it be in their best interests to have the trust, and thus their rights under it, revoked?

**Activity 4.2**

Re-read Penner, Chapter 2: ‘Property, obligations, and trusts’, paras 2.10–2.16 and 2.25, and try to compose a definition of ‘fiduciary duty’.

No feedback provided.

### 4.2.1 Typical dispositive powers and duties

The overarching dispositive duty is, of course, to distribute the trust rights according to its terms. But under the terms of the trust, there may be additional dispositive powers, in respect of which there may or may not be duties. The four most typical dispositive powers are:

- powers of appointment
- powers to appoint individuals to a class of beneficiaries
- the power of maintenance
- the power of advancement.

Persons who might obtain some distribution from the trust only if a discretion is exercised in their favour are generally called the ‘objects’ of the power or discretionary trust.

**Power of appointment**

A power of appointment is a power to distribute rights, but normally with no duty to do so. The person to whom the power is granted is called the donee of the power, and the persons to whom those rights may be distributed are called the objects of the power. When a power of appointment is included in a trust, it is usually the trustees
who have the power to exercise it, but powers to appoint trust assets can also be
granted to donees other than the trustees. A general power is a power to appoint
to anyone in the world, including the donee of the power himself. A special power
is a power to appoint to a specific group of objects or a specified class of objects
(for example, all of the employees of Widgets Ltd). A hybrid power or intermediate
power is a power to appoint to anyone except a specific group or specified class (such
as ‘a power to appoint to anyone except the settlor, his spouse, and the trustee or
employees of the trustee’).

A power to appoint individuals to a class of beneficiaries entitles the holder to add a
named individual to a group which potentially benefits by a distribution of trust rights.
For example, a trust instrument might provide for a discretionary trust of income for
the settlor’s children, with a power granted to the trustees to appoint the settlor’s
nephews and nieces to that class. Sometimes, the holder of a power is under a duty
to exercise it, in which case it is the same as a dispositive duty. For example, a trust
might provide that Alexa is entitled to the income generated by the trust rights for
life, ‘with power by will to appoint the capital amongst her children in such shares as
she in her absolute discretion thinks fit’. On the proper construction of the document,
it may be determined that Alexa was obliged to appoint the capital by her will. Note
that there is still a discretion here since it is up to Alexa to decide how much each of
the children gets, but she is obliged to appoint. As a result, this is properly understood
as a trust to distribute with a discretion to determine individual shares, and is known
as a ‘Burroughs v Philcox trust’, after a case where such a trust arose. If Alexa dies
without exercising the power, the court will direct the distribution of the rights evenly
amongst the objects of the class.

On the other hand, a power may be construed to be exercisable only at the option of
the holder. If the power is personal, the holder may exercise it or not as he sees fit. If
the power is subject to a fiduciary duty, the donee must from time to time consider
whether and how to exercise it with the best interests of the principals in mind.

**ACTIVITY 4.3**

Read *Vatcher v Paull* [1915] AC 372. What is a ‘fraud on a power’? Make a short (not
more than two minutes) spoken presentation in answer.

### 4.2.2 The powers of maintenance and advancement

These powers are related. The power of maintenance relates to income while the
power of advancement relates to the capital. They are always held by trustees and
are therefore fiduciary. Note that these powers can only be exercised by trustees.
A stranger to whom the rights are transferred in breach of trust, though obliged to
return the rights, is not a trustee in the full sense of the word, and so does not have the
duties and powers of a trustee thereby vested in them. They are a bare trustee, whose
only duty is to return the rights received.

**Power of maintenance**

A power of maintenance is a discretion given to the trustees to apply the income
generated by the trust rights for the benefit of an infant beneficiary. This power is
provided by s.31 of the Trustee Act 1925, unless it is expressly or implicitly excluded
by the terms of the trust. Alternatively, it may be expressly conferred by the trust
instrument which will determine how it may be used.

There are complex preconditions for the exercise of the power of maintenance, which
arise out of a concern to achieve fairness amongst the different (classes of)
beneficiaries under the trust. The income from which the maintenance payments
may be made must arise from capital in which the beneficiary who is to receive the
payment’s interest is already vested. If the beneficiary has a vested interest in the
capital, the gift is said to ‘carry’ the intermediate income and this carried income
is available to be paid in maintenance, unless the instrument discloses a contrary
intention, such as where the income is given to some other person or possession of it
is to be deferred to some future date.
A beneficiary under a discretionary trust does not have an interest in capital sufficient to permit maintenance payments of income (Re Vestey’s Settlement (1950) 2 All ER 891) but contingent gifts generally carry the intermediate income (subject to several expectations).

Where the preconditions exist, the trustees may use as much of the income as they think fit. The remainder is accumulated either to be used for future maintenance or to be dealt with as if it is capital according to s.31(2). One should also note the possibility of the court, in the exercise of its inherent jurisdiction, authorising maintenance out of capital where there is no other means for an infant’s support: Wellesley v Wellesley (1839).

Under s.31(1)(ii) of the Trustee Act 1925, if an infant attains the age of majority but still has only a contingent interest in the capital, the trustee is bound to pay any available income to him, unless there is a contrary intention in the instrument, such as duty to accumulate the income: Re Turner’s Will Trusts [1937] 1 Ch 15.

**Power of advancement**

A power of advancement allows trustees to pay or apply capital for the benefit of a beneficiary who is an infant or merely has a future or contingent interest. As with maintenance, the power may be created expressly, or trustees may rely on the statutory power in the Trustee Act 1925, s.32 unless that power is excluded by the trust instrument.

Examine the terms of s.32 carefully, and note the following matters, which are expanded on in the cases:

- The broad meaning of ‘advancement or benefit’ of the beneficiary is illustrated in cases such as Pilkington v IRC [1964] AC 612 HL; Re Clore’s Settlement Trusts [1966] 2 All ER 272; and Re Pauling’s Settlement Trusts [1964] Ch 303.

- Advancement may be by way of resettlement on new (tax-efficient) trusts (Pilkington), provided this does not infringe the rule against remoteness of vesting. Note also the limits on the power contained in s.32(1), especially the need to obtain the consent of persons whose interests may be prejudiced, and the types of trust rights to which the power applies, listed in s.32(2).

- It appears to be undecided whether the new trusts can be discretionary trusts.

- The trustee may have some obligation to see that the money is actually used for the benefit of the beneficiary: see Re Pauling’s Settlement Trusts.

**ESSENTIAL READING**

- Trustee Act 1925 ss.31, 32.
- Cases: Pilkington v IRC [1964] AC 612 (HL); Re Pauling’s Settlement Trusts [1964] Ch 303 (CA).

At least one of the following:

- Oakley, Chapter 17: ‘Income from the trust fund’, Section IV ‘The maintenance of minor beneficiaries’; Chapter 18, ‘Applications of trust capital’.

**FURTHER READING**


**Activity 4.4**

Draw up a list of considerations you would bring to bear in deciding whether, and how much, of the trust fund to distribute to a beneficiary under (a) a power of maintenance and (b) a power of advancement.
Summary

The powers of maintenance and advancement allow the trustee to depart from the strict structure of the trust to deal with the needs of minor or younger beneficiaries. The former allows the trustee to advance income which would otherwise be accumulated during minority on the monthly living expenses of a minor beneficiary, while the latter allows the trustee to pay portions of capital to a beneficiary in advance of the time they would otherwise receive it, usually to help the beneficiary get started (i.e. advanced) in adult life. Both powers are provided for by statute, though trust instruments may and typically do expand on these powers. The power of advancement applies only to the income arising on property in respect of certain dispositions of trust rights, those which ‘carry’ the intermediate income. The power of advancement is read widely to include an advancement by way of making a further settlement.

4.3 Typical administrative powers and duties

Trustees must keep the trust rights separate from their own and keep trust accounts (i.e. maintain proper records of their transactions with the trust rights). Trustees typically also have a power to invest the trust rights to exchange cash and other trust rights such as shares to achieve a portfolio of rights which will produce a reasonable return at a reasonable risk. If so, they also have a duty to invest with due care, exercising or drawing upon investment expertise. Trustees typically have the power and duty to insure rights held by the trust. They usually have the power to delegate their administrative functions to agents for the better administration of the trust, but have a duty to monitor their agents’ performance. Trustees may have powers to appoint new trustees (see Chapter 14), to seek the variation of a trust (Chapter 15) and to ‘export’ the trust to other jurisdictions (usually for tax reasons). Trustees have a general duty to apply to the court whenever there is a problem with the administration of the trust which cannot be resolved without the court’s assistance.

Persons other than trustees may have administrative duties. A settlor might give himself or others a power to replace the trustees, to change the jurisdiction in which the trust is administered, or to veto certain investments. Such powers tend to be seen as fiduciary to the beneficiaries, whether the holder is a trustee or not, on the basis that administrative powers are to be exercised for the better administration of the trust, and the trust is to be administered for the benefit of the beneficiaries.

4.4 Investment

If the trustees have a power to invest trust rights, this carries with it the duties (a) to preserve the overall value of those rights and (b) to be ‘even-handed’ between the different classes of beneficiaries. In many trusts, there will be income beneficiaries and capital beneficiaries.

4.4.1 Even-handedness

Some investments (such as gold and antiques) produce no income, though they may themselves increase in capital value. Other investments will be all income (i.e. what are called ‘wasting assets’, such as a 20-year lease in which all the value comes from the rent). Clearly, then, a trustee may favour income beneficiaries at the expense of capital beneficiaries, or vice versa, by making particular kinds of investments. Equity imposes a duty of even-handedness, which requires the trustee to balance these interests fairly when making investment decisions.

4.4.2 Risk versus return in investment choices

The two chief characteristics of any investment are risk and return. These are directly related: the greater the risk of loss, the greater the percentage return on capital any investor will demand. Traditionally equity favoured safety over high return. Trust instruments themselves almost always empower the trustee to invest in a wide range
of more or less risky investments. Historically, investment clauses were interpreted restrictively, but now are given their plain meaning: Re Harari’s Settlement Trusts [1949] All ER 430. If there is no express investment clause, the statutory regime provided by the Trustee Act 2000 governs the trustee’s investments.

4.4.3 The Trustee Act 2000

Prior to 1 February 2001, the Trustee Investments Act 1961 governed the trustee’s duty of investment unless the trust instrument provided otherwise, and it imposed inconvenient restrictions upon investment. The Trustee Act 2000 now governs unless the trust instrument provides otherwise. It (a) gives the trustees very broad powers of investment, but (b) imposes on them a duty of care to ensure that the power is used prudently.

Section 3 of the Act provides a general power of investment by which a trustee may make any kind of investment that they could make if they were absolutely entitled to the trust rights. That is, they may make any investment they could make if the rights were held by them outright.

Section 8 gives the trustee a power to acquire titles to land in the UK, even if the land is not to be used to generate rental income but to provide a home for one or more of the beneficiaries. This separate treatment of land is a reaction to the past. In Re Power (1947), trustees were barred from buying land to provide a house in which the beneficiaries could live.

Section 1 of the Act provides for a general duty of care applicable to trustees, and by schedule 1, this duty applies to the trustee when exercising any power of investment, either under the statute or conferred by the trust instrument (though the duty of care may be ousted by the trust instrument). Section 1 provides that the trustee must exercise:

such care and skill as is reasonable in the circumstances, having regard in particular to (a) any special knowledge or experience that he has or holds himself out as having, and (b) if he acts in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession.

Section 4 requires the trustee when exercising any power of investment to have regard to the ‘standard investment criteria’, and to review the investments from time to time with these criteria in mind. The standard investment criteria are (a) the suitability of particular kinds of investment for the trust, and (b) the need for diversification of the trust investments. According to modern investment theory, investors should balance the risks of particular investments against the risks of other investments. Savings bonds generally perform well when inflation is low, whereas gold generally holds its value in times of high inflation. Buying both allows the investor to offset the inflation-sensitive risks of one against the other. Thus the modern prudent investor is to be judged not by the individual investment vehicles they choose but on the overall ‘portfolio’ of investments.

Section 5 of the Act also requires the trustee, before exercising any power of investment, to take advice from someone the trustee reasonably believes is able to provide proper advice of this kind by virtue of their ability and experience in such matters, unless it would be reasonable in the circumstances to forgo such advice. (Presumably it would be reasonable not to seek advice in the case of a trust with very limited funds, or a trust of short duration, for which the only sensible option might simply be to put the money in a bank.)

4.4.4 The standard of prudence in making trust investments

A standard of prudence, just like the standard of care in the law of negligence, cannot be spelt out in advance by a set of rules, but dictates reasonable behaviour in the circumstances.
ESSENTIAL READING

- Trustee Act 2000.

At least one of the following:

- Oakley, Chapter 14: ‘The administration of trusts’, Section VI ‘Investing the trust property’.
- Pettit, Chapter 17: ‘The investment of trust funds’.

FURTHER READING


ACTIVITIES 4.5–4.7

4.5 Read the cases of Speight v Gaunt [1883] 9 App Cas 1, Re Whiteley [1886] 33 Ch D 347, and Re Chapman [1896] 2 Ch 763 and explain how the standard of prudence applied to the trustees’ actions in those cases.

4.6 Read Re Lucking’s Will Trusts [1967] 3 All ER 726 and Bartlett v Barclays Bank Trust Co Ltd [1980] Ch 515. Do any special considerations apply to the management of investments when the trust has a large or majority shareholding in a particular company?

4.7 Read Nestle v National Westminster Bank [1994] 1 All ER 118. Why did Miss Nestle’s claim fail? What did the court say about the duty of ‘even-handedness’? In the light of this, is the duty of investment an administrative duty, a dispositive duty, or something of both?

4.4.5 Social or ethical investing

Cowan v Scargill (1985) concerned a dispute amongst the trustees of the National Coal Board pension fund for miners. The trustees appointed by the union refused to consent to an investment plan, including overseas investment and investment in industries in direct competition with the coal industry. Megarry V-C held that the refusal of the union trustees was in breach of trust:

When the purpose of the trust is to provide financial benefits for the beneficiaries, as is usually the case, the best interests of the beneficiaries are normally their best financial interests. In considering what investments to make, trustees must put to one side their own personal interests and views. Trustees may have strongly held social or political views. They may be firmly opposed to any investment in South Africa or other countries, or they may object to any form of investment in companies concerned with alcohol, tobacco, armaments or many other things. In the conduct of their own affairs, of course, they are free to abstain from making any such investments. Yet under a trust, if investments of this type would be more beneficial to the beneficiaries than other investments, the trustees must not refrain from making the investments by reasons of the views that they hold.

As Cowan v Scargill is the leading case in this area, one must conclude that social or ethical investing is not currently permitted for most trusts, though the issue is a matter of controversy amongst writers on trusts.

ACTIVITY 4.8


Critically examine the arguments for and against social or ethical investment by trustees.
Summary

The Trustee Act 2000 has greatly simplified the law on the investment of trust funds (though professionally drawn trust instruments are likely to continue to provide the trustees with wide investment powers). First, it provides extremely wide scope for investment in terms of the sorts of investment a trustee may undertake, but controls this by imposing a general duty of care on investing, appropriate to the expertise of the trustee. Trustees may not let their own ethical or political views govern their advice of investments.

4.5 Power of delegation

By subs.11(1) and (2) of the Trustee Act 2000, trustees may collectively delegate any of their functions to an agent except:

- any function relating to whether or in what way any trust rights should be distributed
- any power to decide whether any fees or other payment to be made out of trust rights should be made out of income or capital
- any power to appoint a person to be a trustee of the trust, or
- any power conferred by any other enactment or the trust instrument which permits the trustees to delegate any of their functions or to appoint a person to act as a nominee or custodian.

The trustees may delegate tasks to one of themselves (s.12(1)), though not to any trustee who is also a beneficiary (s.12(3)). By s.15, where the agent is to carry out any ‘asset management functions’, such as investment, the trustees must first provide a written ‘policy statement’ to guide the agent’s exercise of their powers in the best interests of the trust, for example, so that the investments provide sufficient income to meet the level of provision the trustees intend for the income beneficiaries. By s.22 the trustees are required to review any delegation arrangements, and to consider revising the policy statement. By Schedule 1, para.3, the s.1 duty of care applies to the trustees’ appointment of agents and their review of them under s.22.

By s.25 of the Trustee Act 1925 any individual trustee may, by power of attorney, delegate any or all of their duties, powers or discretions, whether administrative or dispositive, for up to 12 months. Under s.25(4), the trustee must inform in writing any person entitled to appoint new trustees under the trust and all the other trustees, which allows them to consider whether the delegation trustee should be replaced. The trustee is liable under s.25(7) for all acts and defaults of their delegate by power of attorney as if they were their own acts or defaults.

Essential reading

- Trustee Act 2000.
- Trustee Act 1925, s.25 (as amended).
- At least one of the following:
  - Pettit, Chapter 20: ‘Appointment of agents, nominees, and custodians – delegation of trusts’.

Further reading

**ACTIVITY 4.9**

Make a short spoken presentation on the following:

‘Under what circumstances would it be prudent, as a trustee, to delegate one’s power of investment?’

**Summary**

The Trustee Act 2000 gives trustees wide powers to delegate their ‘administrative’ functions, though not their dispositive discretions or other powers which would appear to require the judgment of a trustee as to what is in the best interest of the beneficiaries as a whole, for example, the appointment of successor trustees. By s.25 of the Trustee Act 1925, a trustee may delegate their rights, duties and powers as a trustee for a limited time.

### 4.6 Interests of beneficiaries and objects of powers

The right of a beneficiary under a fixed trust is a right which can be assigned and will vest in the beneficiary’s trustee in bankruptcy in the event of the beneficiary’s insolvency (except in the case of protective trusts, as discussed above). By contrast, discretionary trust beneficiaries have no right to receive anything at all, and so have nothing to assign. They have only a hope (spes) of receiving some of the trust rights. They do, however, have a right to be considered and a right to due performance of the trust, which they can enforce against the trustees. In the case of general or hybrid powers, the objects have no rights whatsoever, since the class of objects amounts, essentially, to the whole world, or in the case of hybrid powers, the whole world minus a few. Those entitled in default of appointment will only have the right to ensure that the power is not improperly exercised. The individual objects of special powers are in a similar position to the objects of a discretionary trust. They can enforce the power by ensuring no invalid appointments are made, and where the power is fiduciary (as when held by a trustee), they can insist upon the trustee properly considering its exercise, though they cannot, of course, insist upon any appointments.

#### 4.6.1 Rights and powers of objects

[There is an irreducible core of obligations owed by the trustees to the beneficiaries and enforceable by them which is fundamental to the concept of a trust. If the beneficiaries have no rights enforceable against the trustees, there are no trusts. (Millett LJ in Armitage v Nurse [1997] EWCA Civ 1279, [1998] Ch 241, 253)]

The ability of the beneficiaries actually to require recalcitrant trustees to perform the trust is the *sine qua non* of an effective trust. The beneficiaries are able to require them to carry out the trust properly according to its terms, and can sue the trustees for breach of trust or third parties who knowingly receive trust rights dissipated in breach of trust or dishonestly assist in a breach of the trust.

#### 4.6.2 Beneficiaries’ right to be informed of their interests under the trust

According to *Hawkesley v May* [1956] 1 QB 304 beneficiaries whose interests are vested rather than contingent on the happening of a certain event have a right to be informed of the fact that they have a right under the trust, and it is within the court’s discretion in an appropriate case (namely, where it is reasonable to assume that such beneficiary had a genuine likelihood or expectation that a dispositive discretion might be exercised in their favour) to require settlors to provide the names and addresses of trustees even to a discretionary beneficiary: *Murphy v Murphy* (1998).
4.6.3 Beneficiaries’ right to information

In order to monitor the trustees’ conduct of the trust and hold them to account if they breach the trust, the beneficiaries must be able to obtain information about the running of the trust from the trustees. It is now generally accepted that genuine beneficiaries, whether of a fixed or discretionary trust (Chaine-Nickson v Bank of Ireland [1976] IR 393; Spellson v George [1987] 11 NSWLR 300), and perhaps even of a contingent interest (Armitage v Nurse [1998] Ch 241 per Millett LJ) are entitled to copies (made at their own expense) of the trust accounts and all trust documents and such rights cannot be limited by contrary provisions in the trust instrument on pain of rendering the trusts in their favour invalid (on Armitage principles, above). On the other hand, it has been asserted that objects of powers of appointment (i.e. powers that the donee is under no duty to exercise, whether fiduciary or personal) are not entitled to see the trust documents. The Privy Council advised in Schmidt v Rosewood Trust [2003] UKPC 26, [2003] 2 AC 709 that the objects’ rights to information reflects equity’s insistence that the trust is properly administered. Whether discretionary beneficiaries or objects of powers have rights to information will turn on the circumstances of the case, in particular on the likelihood of enforcement by other categories of beneficiary or object under the particular trust. In Re Londonderry’s Settlement [1965] Ch 918, the Court of Appeal held that beneficiaries, while entitled to see all other trust documents which record the trustees’ dealings with the trust property, are not entitled to see documents which disclose their reasons for exercising a dispositive discretion in favour of one or some beneficiaries rather than others, as this would inhibit them in taking such decisions, and might lead to strife amongst the beneficiaries.

4.6.4 Beneficiaries’ rights under the principle in Saunders v Vautier

The beneficiaries, if of full age and sound mind, may consent to the trustees acting outside the terms of the trust (i.e. doing what would otherwise be a breach of trust), and may consent to the variation of the terms of the trust if they are minded so to do. The principle, named after the case of Saunders v Vautier (1841), although of much longer standing, is the logical extension of this fact, and may be stated as follows: if a beneficiary with an absolute interest under a trust is sui juris and of sound mind, they may call for a transfer of the trust rights which represent that interest, and the trustees are obliged to transfer them to the trustee; if the trustee is a sole beneficiary, this will result in the complete collapse of the trust. Thus if under a trust, Amy is to receive the income generated by trust rights until she is 30, at which time she is to receive the capital, she can demand a transfer of the rights as soon as she reaches 18.

Under fixed trusts, the right of sui juris beneficiaries to call for a transfer of trust rights is subject to a general limitation that such a transfer must not result in the devaluation of the other beneficiaries’ shares.

In general, the [individual sui juris beneficiary] is entitled to have transferred to him... an aliquot [i.e. ‘proportionate’]… share of each and every asset of the trust fund which presents no difficulty so far as division is concerned. This will apply to such items as cash, money at the bank or an unsecured loan, Stock Exchange securities and the like. However, as regards land, certainly, in all cases, as regards shares in a private company in very special circumstances... the situation is not so simple, and even a person with a vested interest in possession in an aliquot share of the trust fund may have to wait until the land is sold, and so forth, before being able to call upon the trustees as of right to account to him for his share of the assets. (Stephenson v Barclays Bank Trust Co Ltd (1975) per Walton J.)

In the case of discretionary trusts, the principle only operates when all of the discretionary beneficiaries together call for the rights which, taken together, are held on trust to be distributed amongst them: Re Smith [1928] Ch 915. In other words, such beneficiaries may together call upon the trustees to transfer the trust rights to them as co-owners. Following McPhail v Doulton (1970), the law has allowed setters to create discretionary trusts where the class of beneficiaries is so large as to be unlistable (for example, ‘all the employees and ex-employees of the University of London and their relations’), and in these cases it is obvious that all the objects of the discretionary trust will not be able to combine to call for the collapse of the trust.
Summary

The beneficiaries are entitled to enforce the trust against the trustees. If no one has any rights to enforce any trust against the right-holder, then the latter is not a trustee and there is no trust. Following on from this principle is the right of beneficiaries to be informed that they are beneficiaries, and to information from the trustee as to the carrying out of the trust. However, not all beneficiaries or objects of the trust of whatever kind of interest (discretionary, contingent, and so on) have equal rights to information, and the decision of the Privy Council in *Schmidt v Rosewood Trust Ltd* indicates that much depends on the circumstances of the particular trust, though the court will insist that sufficient access to information be granted to allow the trust to be enforced. Under the principle of *Saunders v Vautier*, beneficiaries may call for a conveyance of trust rights, though only collectively in the case of discretionary trusts, and in every case only where to do so would not detrimentally affect the interests of the other beneficiaries.

**SAMPLE EXAMINATION QUESTIONS**

**Question 1** Under the terms of a settlement, a fund of personal property worth £150,000 is held by trustees upon trust in equal shares for such of the settlor’s grandchildren, Tom, Dick and Harriet, as attain the age of 25. Tom is now 25, Dick is 18, and Harriet is 13. Advise the trustees:

a. whether they may now distribute one third of the capital of the trust fund to Tom;

b. whether they should distribute any, and if so what, trust income and to whom;

c. whether they may advance the sum of £25,000 out of capital to enable Dick to train for a commercial pilot’s licence;

d. whether they may pay out of trust monies the school fees of Harriet, who is about to go to boarding school.

**Question 2** Tim and Toby are the trustees of a large trust fund held on behalf of the Evangelical Christian Church of Yorkshire. The trust originated informally, and there is no specific provision in the trust terms concerning investments. Tim and Toby propose the following investment plan: (1) to put half the funds in a building society account; (2) to purchase a 50 per cent stake in a local computer technology company of which Tim has heard good things; and (3) to invest the rest in a financially stretched company which produces Christian literature. Advise Tim and Toby.

**Question 3** ‘The range of sound investments available to trustees is so extensive that very frequently there is scope for trustees to give effect to moral considerations … without thereby prejudicing beneficiaries’ financial interests. In practice, the inclusion or exclusion of particular investments or types of investment will often be possible without incurring the risk of a lower rate of return or reducing the desirable spread of investments. When this is so, there is no reason in principle why trustees should not have regard to moral and ethical considerations, vague and uncertain though these are. The trustees would not be departing from the purpose of the trust or hindering its fulfilment.’ Lord Nichols (1995), speaking extra-judicially. Discuss.

**Question 4** ‘The beneficiaries’ rights to inspect trust documents are now seen to be better based not on equitable proprietary rights but on the beneficiaries’ rights to make the trustees account for their trusteeship.’ (Hayton, quoted in *Re Rabaiotti’s 1989 Settlement*.) Discuss.

**Question 5** What are the principles governing the trustee’s power to delegate under the Trustee Act 2000?

**Question 6** ‘There is no point in speaking in general terms about the ‘beneficiary’s rights’ under a trust – it all depends what specific position the beneficiary is in’. Discuss.
ADVICE ON ANSWERING THE QUESTIONS

Question 1

a. Having attained the age of 25, Tom is now entitled to his capital interest of £50,000 (though his interest may increase if one or both of his siblings fail to attain the age of 25), unless the present sum has been diminished by advancements made to him in the past, which will correspondingly reduce his share. Answers should also explain, making reference to the appropriate provisions of the Trustee Act 1925 and the case law, that Tom will also be entitled to any accumulated income representing income from his share of the capital.

b. See (a) regarding accumulated income for Tom. Section 31(1)(ii) of the 1925 Act should be applied to determine Dick's position (trustees must now pay him income on his presumptive share) and s.31(1)(i) to Harriet's case.

c. Assuming no prior advancements to any grandchild, £25,000 is one-half of Dick's presumptive share of the capital, and under s.32(1)(a) may be advanced to him; however, an advancement of this amount will disentitle him from any further advancements, and that needs to be taken into account.

d. Under s.31(1)(i) the trustees may do so – a good answer will state the general way in which maintenance payments are accounted for, in particular that income undistributed may be accumulated and used to maintain an infant in later years prior to the infants' reaching 18.

Question 2

The first thing to note is that the investment of the trust rights will be governed by the Trustee Act 2000, as there is no specific investment provision. A good answer will go through the relevant provisions of the Act, in particular the need for diversification and the duty to seek investment advice. As to the specific provisions of Tim and Toby's plan, the whole looks very poorly diversified.

1. Does not look to provide a good return, but may be justified if the trustees foresee drawing on the fund in large amounts in the near future.

2. Looks hazardous, and the case law concerning trustees' duties where the trust holds a controlling interest in a company must be considered.

3. Raises the issue of 'ethical' investing by a charity, and Harries v Church Commissioners (1992) and the surrounding academic debate on ethical investing is relevant.

Question 3

This question deals with 'ethical' (or 'social') investment of trust funds. Cowan v Scargill must be discussed to reveal the background principles of law upon which Megarry V-C relied in opposing the application of ethical standards to trustee investments. Lord Nichols appears to suggest that there ought to be a limited scope for such investing, investing ethically only to the extent that the risk and return profile of the trust fund is not imperilled. Is this a practicable stance to take? Why should the trustee have the power to choose the ethical standards to apply (as opposed to the settlor, who can include them if they want when they create the trust, or the beneficiaries, who can, if of full age, consent to departures of the trust instrument). (See Penner, Chapter 10, paras 10.22–10.31.) Whether similar considerations ought to apply to charitable trusts given their special function might be discussed, and if so, Harries v Church Commissioners for England (1992) must be considered.

Question 4

A good answer must discuss the relevant case law, both with respect to which possible objects of a trust have a legitimate right to see the 'trust accounts' and the 'trust documents', and with respect to which documents beneficiaries are entitled to see, with regard to beneficiaries of a fixed or discretionary interest: Chaine-Nickson v Bank of Ireland (1976), Spellson v George (1987); with regard to those with contingent interests: Armitage v Nurse (1998) per Millett LJ; with regard to objects of mere powers: Schmidt v Rosewood Trust Ltd (2003). The quotation states that the law has generally undergone a shift in regarding the beneficiaries' rights to information as flowing from their proprietary interest in the trust to seeing such rights as flowing from their right to make the trustees account for their stewardship of the trust, which
is one way of reading *Re Londonderry’s Settlement* (1964); *Re Rabaiotti’s 1989 Settlement* (2000). The first thing to note about this view is that the enforcement principle suggests that objects in different situations (e.g. discretionary beneficiary, income or capital beneficiary) should only be entitled to such information as is relevant to the enforcement of their own particular interest, and this appears to have been considered correct by Hoffmann J at first instance in *Nestle v National Westminster Bank* (1988), where the capital beneficiary was not entitled to see the accounts disposing of the income to income beneficiaries. The student should consider whether *Re Rabaiotti’s 1989 Settlement* takes the law in a different direction, from the principle that beneficiaries’ rights in this respect arise so as to permit them to enforce their rights against the trustee, to the idea that beneficiaries should be entitled to such information only when it is ‘in their best interests’, and the facts of *Re Rabaiotti* should be discussed.

**Question 5** A straightforward question requiring an outline of the principles upon which the Trustee Act 2000 empowers trustees to delegate their functions. Particular reference should be made to provisions concerning the trustee’s duty of care in selecting and monitoring agents. Consideration should also be given to the rationale for the Act not permitting delegation of certain tasks, and to its more extensive directions concerning the delegation of the investment of trust funds. A good answer will review briefly the history of the law of delegation, in particular the perceived flaws in the provisions under the Trustee Act 1925, to provide a context for understanding the 2000 Act provisions.

**Question 6** Another straightforward question, requiring a discussion of how the position of a beneficiary of a fixed interest under a trust, an object of a discretionary trust, and the object of a mere power differ with respect to: (a) their ability to enforce the trust against the trustees; (b) their rights to information; (c) their *Saunders v Vautier* rights, and whether these differences are coherent and justifiable. A good answer will consider the case of discretionary trusts with unlistably broad object classes. A very good answer will also consider the question of which beneficiaries have ‘vested’ interests under the trust for various purposes in law, such as the law of taxation – see *Gartside v IRC* [1968] AC 553; *Re Weir’s Settlement* [1969] 1 Ch 657; *Sainsbury v IRC* [1970] Ch 712; *Re Trafford’s Settlement* (1915).
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

| I can describe the structure of the typical express trust by setting out the rights the beneficiaries have, and the powers and duties that the trustees, and others, may have. |
| Ready to move on | Need to revise first | Need to study again |
| ☐ | ☐ | ☐ |

| I can explain in outline the beneficiaries’ rights to follow and trace rights held on trust that have been transferred in breach of trust and the significance of the term ‘equity’s darling’. |
| Ready to move on | Need to revise first | Need to study again |
| ☐ | ☐ | ☐ |

| I can set out the typical sorts of administrative and dispositive powers and duties a trustee will have. |
| Ready to move on | Need to revise first | Need to study again |
| ☐ | ☐ | ☐ |

| I can describe in detail the law governing the powers of maintenance and advancement, the duty of investment, and the power of delegation. |
| Ready to move on | Need to revise first | Need to study again |
| ☐ | ☐ | ☐ |

| I can explain the rights of objects to information under the rule in Saunders v Vautier. |
| Ready to move on | Need to revise first | Need to study again |
| ☐ | ☐ | ☐ |

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

| 4.1 Introduction to rights and duties | Must revise | Revision done |
| ☐ | ☐ | ☐ |
| 4.2 Powers and duties of trustees and others | ☐ | ☐ |
| 4.3 Typical administrative powers and duties | ☐ | ☐ |
| 4.4 The duty of investment | ☐ | ☐ |
| 4.5 Power of delegation | ☐ | ☐ |
| 4.6 Interests of beneficiaries and objects of powers | ☐ | ☐ |
5 Creating express trusts I: the declaration of trust

Contents

Introduction ........................................... 48

5.1 Intention to create a trust ........................ 49

5.2 Identifying the rights .............................. 52

5.3 Identifying the beneficiaries ..................... 54

Reflect and review ................................. 60
Introduction

A necessary, though not always sufficient, condition for the creation of an express trust is the expression of an effective intention to create a trust. Where the settlor does not intend to be the trustee, a further requirement is that the rights which are to form the subject-matter of the trust are vested in the persons who will act as trustees. This is known as the 'constitution' of the trust, and is dealt with in Chapter 6. In cases where the settlor himself is to be the trustee, no such constitution is necessary, for the rights are already where they need to be. But in such cases, an effective declaration is still necessary. This chapter is concerned with the elements such a declaration must contain.

It is vital that you keep the matters to be covered in this chapter, which are issues of the substantive requirements of a valid trust, separate from those in the next two chapters, which consider issues of the constitution of the trust and proof of the declaration of trust. One of the most common mistakes made by students (and even some judges) is to confuse these three issues. To make any sense of trusts, you need to be able to tell whether a particular question involves problems of substance, constitution, or proof.

There are three points which need to be appreciated at the outset. The first is that only manifestations of intent count. The mere fact that a right-holder has an intention to create a trust but which the right-holder keeps to themself will not cause a trust to come into being. There can be no express trust unless the intention is made manifest (i.e. expressed). As Megarry J said in *Re Vandervell's Trusts (No 2)* [1974] Ch 269, 294, ‘the mere existence of some unexpressed intention in the breast of the owner of the property does nothing: there must at least be some expression of that intention before it can effect any result.’ Also see *Byrnes v Kendle* [2011] HCA 26, 243 CLR 253.

The second is that the intention will probably only be found from words, either spoken or written. Although the expression of an offer and acceptance in the context of a contract can sometimes be deduced from mere conduct alone, as, for example, where I walk into a shop and hand the shopkeeper cash in exchange for a newspaper, neither of us speaking any words, the concept of a trust is too complex to be expressed otherwise than by words.

The third is that the test of construction of the manifested intent, just as it is in contract, is objective. What is relevant is not what the speaker meant by the words, but what a reasonable person hearing those words would have thought they meant. So, for example, it is normally irrelevant that the speaker was telling a deliberate lie when they manifested an intent to hold rights on trust for another. This was made clear by Lord Diplock in *Gissing v Gissing* [1970] UKHL 3, [1971] AC 886, 906, where he said:

> As in so many branches of English law in which legal rights and obligations depend upon the intentions of the parties to a transaction, the relevant intention of each party is the intention which was reasonably understood by the other party to be manifested by that party's words or conduct notwithstanding that he did not consciously formulate that intention in his own mind or even acted with some different intention which he did not communicate to the other party.

There are five substantive requirements of a valid declaration of trust:

1. The intent which is expressed must show that the settlor intended to create a trust.
2. The rights which are to form the subject-matter of the trust have been identified.
3. The persons who are to be the beneficiaries of the trust have been identified.
4. The shares in which such beneficiaries are to be entitled under the trust have been identified.
5. The trust is workable by the trustees.

The chapter assumes that you know by now the difference between a fixed trust, a discretionary trust, and a power of appointment. These institutions were introduced in Chapter 3, which you should now re-read.
5.1 Intention to create a trust

5.1.1 The requisite intention

The vast majority of trusts come into being because the law responds to a manifestation of intent by a right-holder to create a trust of that right. As we have seen, we call such a person the ‘settlor’. The first substantive requirement for a valid declaration of trust is that the words expressed by the alleged settlor manifest such an intention. As a matter of construction, it will need to be shown that the settlor intended to subject the holder of the right (be it himself or the person to whom that right is transferred) to an obligation enforceable in a court of law that the right be held on behalf of another. The imposition of a moral (i.e. non-legal) obligation, sometimes called an ‘obligation binding in conscience alone’, is not sufficient. As Christian LJ said in *McCormick v Grogan* (1867) 1 IR Eq 313, ‘The real question is, what did [the settlor] intend to be the sanction? Was it to be the authority of a court of justice, or the conscience of the devisee?’

This issue usually arises on a gratuitous transfer of rights, where the question becomes, ‘Was the recipient intended to take those rights absolutely (e.g. as a gift) or to hold them for another (i.e. as a trustee)?’ In *Re Adams & Kensington Vestry* (1884) 27 Ch D 394 the testator left his whole estate to his wife ‘in full confidence that she will do what is right as to the disposal thereof between my children, either in her lifetime or by will after her decease’. During her lifetime, the widow attempted to give some of the rights away outside her immediate family. The Court of Appeal held that she was entitled so to do. There had been no declaration of trust because it was clear that the testator did not intend to impose any legally enforceable obligation on her. He had instead left the matter to her ‘conscience’.

Exactly the same question needs to be asked about situations in which it is alleged that a right-holder has made a self-declaration of trust. The cases show that a mere intention to benefit another person is not enough. In *Jones v Lock* (1865) LR 1 Ch App 25 a father handed a cheque for £900 (made out to himself) to his infant son, saying ‘I give this to baby for himself’. The act was insufficient to transfer the right to sue on the cheque, for such a right only passed at that time by means of an endorsement to the cheque (in the son’s name, in this instance). The father died very soon afterwards, leaving all his personal rights to his family by his first marriage. On behalf of the infant, it was argued that the father had declared himself a trustee of the right to sue on the cheque, so that there was a trust created in favour of the infant during the father’s lifetime. The argument was rejected. Lord Cranworth LC said:

I should have every inclination to sustain this gift, but unfortunately I am unable to do so; the case turns on the very short question whether Jones intended to make a declaration that he held the [right] in trust for the child; and I cannot come to any other conclusion than that he did not.

As we shall see in Chapter 6, the same thinking applies when it is argued that failed attempts to transfer rights to others should be construed as self-declarations of trust.
As both *Milroy v Lord* (1862) 4 De GP & J 264 and *Richards v Delbridge* (1874) LR 18 Eq 11 demonstrate, such arguments are routinely rejected by the courts.

What words then are most appropriate for expressing the intention to create a trust? As we have said, it must be shown that the transferor intended that the recipient (or the transferor in the case of a self-declaration of trust) will be legally obliged to hold the rights in question for another. The clearest expression of such an intent will be found in the use of the word ‘trust’ (‘I give all my estate to my wife to hold on trust for our children’), although in some contexts, other words may serve as well, for example ‘the money in the bank is as much yours as it is mine’: *Paul v Constance* [1976] EWCA Civ 2, [1977] 1 WLR 527 CA, [1977] 1 All ER 195. Note for future reference that the trust in that case was rightly held to be express.

A borderline case?

A case taking a generous approach to the issue of finding a self-declaration of trust was *T Choithram Int SA v Pagarani* [2000] UKPC 46, [2001] 1 WLR 1, [2001] 2 All ER 492.

The deceased, an extremely wealthy businessman, wanted to give his vast fortune to a ‘foundation’, which would then distribute it for various good works. English law knows no concept of a ‘foundation’, which is essentially a continental European idea. The nearest English equivalent is a corporation with charitable objects. However, no such body was ever formed. Instead, his legal advisers drew up the documentation for a trust, though the deceased continued to use the language of a foundation. His ‘foundation’ (trust) was to have seven directors (trustees), including himself. During his lifetime, he executed a deed by which he purported to create the ‘foundation’ (trust) and appointed himself a ‘director’ (trustee). Some of the other ‘directors’ also signed this document. The deceased later solemnly declared that he gave all his wealth to the ‘foundation’, but no transfer to the other ‘directors’ (trustees) was ever made. When he died, the question was whether the deceased had created an *inter vivos* trust. If he had not, then his fortune went to his widow under his will.

The courts of first instance and appeal held that there was no trust and that the widow therefore took because the donor had attempted but failed to make an outright gift. The Privy Council disagreed. Although the words were words of outright gift, in their context they were words of gift to the trustees of the foundation to be held by them on trust. Where one of several intended trustees had the trust rights vested in him, he was bound by the trust and under a duty to transfer the trust rights into the names of all the trustees. Although the deceased had not vested the rights in all the trustees of the foundation, he could not resile from his declaration of gift to the trust which he had established and of which he had appointed himself to be a trustee.

The decision is a difficult one, and arguably places too generous an interpretation of the deceased’s words. Even so, it is important to note that the Privy Council does not here see itself as creating an exception to the rule that equity will not perfect an imperfect gift (see Chapter 6), but merely finding, albeit somewhat generously, a self-declaration of trust in a novel circumstance.

5.1.2 Proving the declaration

Even if declaration of trust was made, there is a separate question whether that fact can be proved to the satisfaction of the court. This is a problem of the law of evidence, not the law of trusts, for the same sort of question arises in all instances of litigation. It is discussed, arguably wrongly, in trusts textbooks and courses, only because there are peculiar rules in respect of two types of trust. Although the general rule is that all types of evidence are admissible to prove the fact that a declaration of trust occurred, the legislature in two instances has placed restrictions on the evidence courts are allowed to admit. First, allegations of declarations of trusts of land must be ‘manifested and proved by some writing signed by some person able to declare such trust or by will’: s.53(1)(b) of the LPA 1925. Second, allegations of declarations of trusts in wills must be
5.1.3 Consequences of no proof of intention to create a trust

What happens if it is not established that the supposed settlor intended to create a trust? The one thing which does not happen is that those rights are returned whence they came (compare the case of uncertainty of objects, below). If there has been a transfer, then the transferee will take the rights outright: Re Adams & Kensington Vestry (1884) 27 Ch D 394. Where there is a failed allegation of a self-declaration of trust, then the right-holder simply remains absolutely entitled. Do not be confused here. Re Adams & Kensington Vestry is not a case of a trust ‘failing’ because the husband used the wrong form of words. His expressed intention was not to create a trust at all, but that his wife should merely act according to her ‘conscience’. There is no trust to fail in such circumstances, but merely an allegation that a trust was declared. Unfortunately, this is not always appreciated by judges and commentators.

ESSENTIAL READING

At least one of the following:

- Cases: Milroy v Lord (1862) 4 De GP & J 264; Jones v Lock (1865) 1 LR 1 Ch App 25; Lambe v Eames (1871) 6 Ch App 597; Richards v Delbridge (1874) LR 18 Eq 11; Re Adams & Kensington Vestry (1884) 27 Ch D 394; Re Schebsman [1944] Ch 83; Paul v Constance [1976] EWCA Civ 2, [1977] 1 WLR 527, [1977] All ER 195.

FURTHER READING

- Hayton & Mitchell, Chapter 4: ‘The three certainties’, Section 2 ‘Certainty of intention’.

ACTIVITY 5.1

Read and note the decision in Paul v Constance [1977] 1 WLR 527.

a. What was the plaintiff claiming?

b. What arguments did the defendant use to attempt to defeat that claim?

c. How were those arguments dealt with by the Court of Appeal?

Summary

A manifested intention to create a trust is the first substantive requirement for a valid declaration of trust. For a declaration to have occurred, it must be shown that the words used by the transferor evinced an intention that the recipient be legally obliged to hold the rights in question for another. This is different from the imposition of a moral obligation, which is insufficient to establish a trust. Unfortunately this distinction can cause difficulty. Re Adams & Kensington Vestry highlights this problem. Furthermore, difficulty occurs in situations in which it is alleged that a right-holder has declared himself a trustee, as in Jones v Lock and Paul v Constance. If such an intention cannot be shown, the rights in question will, if there has been a transfer, be taken by the transferee absolutely. Where there is no transfer but only a failed allegation of self-declaration of trust, the right holder will simply remain absolutely entitled.
5.2 Identifying the rights

5.2.1 Types of right

Almost any rights can form the subject-matter of a trust. Although many judges and commentators describe the rights forming the subject-matter of the trust as the ‘trust property’, this catch-all includes all kinds of non-property rights, such as company shares, bank accounts, and so on. These are rights which are enforceable only against specific persons and therefore not, strictly speaking, property rights at all. For example, a bank account (in credit) gives the account holder a right to sue the bank for repayment of the money loaned to the bank, but no one else is obliged to perform that duty. It is for this reason that such rights are normally regarded as personal, not property, rights.

Please note that, in some contexts, assignable personal rights may be described as property. For example, the Insolvency Act 1986 s.436 defines property to include money, goods, things in action, land and every description of property wherever situated and also obligations and every description of interest, whether present or future or vested or contingent, arising out of, or incidental to, property.

Many, though not all, personal rights are assignable. This is not, however, required for the creation of a trust, since the holder of that right, even though they might not be able to transfer it to someone else, could nevertheless make themselves a trustee in respect of it: Don King Productions Inc v Warren [2000] Ch 291. It had there been argued that a trust could not be created of the benefit of a contract which was expressly made non-assignable on the grounds that it would defeat the whole purpose of the non-assignability clause. This argument was rejected by Lightman J at first instance on the ground, inter alia, that a declaration of trust would not prejudice the rights of the obligor. If the contract required any judgment to be exercised, whether by the promisor or the promisee, a declaration of trust could not alter who was to exercise it or how that judgment was to be exercised, or confer the power to make that judgment on the court. This could not be circumvented by an application of the rule in Saunders v Vautier, since it could not apply if the right in question was not assignable. Lightman J’s reasoning on this point was not questioned in the Court of Appeal. Also see Barbados Trust Co Ltd v Bank of Zambia [2007] EWCA Civ 148, [2007] 1 Lloyd’s Rep 495.

5.2.2 Identifying the trust rights

Given that a trust involves holding rights on behalf of another, it follows that it must be possible to identify exactly what rights are to form the subject-matter of the trust. If we cannot do this, the trustees cannot do their job. Suppose, for example, I have 100 bottles of wine in my cellar and declare that I hold 50 of them on trust for you. There can be no trust until I have identified exactly which 50 bottles I am talking about. Until that is done, if a bottle breaks, is stolen or goes off, it is impossible to say whether it was a bottle which I held on trust for you or owned by me absolutely. For this reason, a claim to be the beneficiary of a trust of bottles of wine failed in Re London Wine Co (Shippers) Ltd [1986] PCC 121. There is nothing mysterious about this, and it applies equally to attempts to sell rights as it does to declarations of trust. As Lord Mustill observed in Re Goldcorp [1994] UKPC 3, [1995] 1 AC 74, the rule is not some arbitrary creation of the judge but is founded on the nature of things.

A trust failed for a different reason in Palmer v Simonds (1854) 2 Drew 221, 61 ER 704, a case involving an attempted testamentary trust of the ‘bulk’ of the testator’s estate. This was a case of what might be called ‘conceptual uncertainty’, the problem being uncertainty as to the meaning of the word ‘bulk’. It is therefore different from the example of the wine bottles where, though we know what 50 bottles means, we do not know which 50 are referred to.

Palmer v Simonds should be contrasted with Re Golay’s WT [1965] 1 WLR 969, which upheld a testamentary trust to provide a ‘reasonable income’ to a beneficiary during her lifetime. The difference here was that the court was able to determine what was reasonable by reference to the beneficiary’s previous standard of living.
A common error that students make with regard to certainty of subject-matter is in relation to a testator’s residuary estate. Note that there is nothing uncertain about a residuary estate, which is simply everything left after the satisfaction of specific legacies in the will. That which is capable of being ascertained, even though not currently ascertained, is not uncertain.

A testamentary trust takes effect after the estate has been administered and the executors (or administrators) allocate the assets to the trust, at which time the subject of the trust will be certain. Since they are under a duty to constitute the trust according to the testator’s instructions, there is no problem with certainty of subject matter, so long as the testator’s instructions are clear.

The topic of certainty of subject-matter was thrown into confusion by the decision of the Court of Appeal in Hunter v Moss [1993] EWCA Civ 11, [1994] 1 WLR 452, [1994] 3 All ER 215 (leave to appeal dismissed [1994] 1 WLR 614 (HL)). The defendant, Moss, made a voluntary (i.e. gratuitous) declaration that he held 50 of his 950 shares in a particular company on trust for the plaintiff. He failed, however, to identify which 50. When the plaintiff later tried to enforce the trust, Moss, relying on Re London Wine, argued that it failed for uncertainty of subject-matter. Dillon LJ in the Court of Appeal distinguished London Wine on the ground that shares were intangible whereas bottles of wine were not. He held that the trust was valid because, as each share carried identical rights, it did not matter which 50 were held on trust. This, however, is doubtful. The difficulty is that it does not provide an answer to the problem of dealings by someone in the position of Moss. Suppose he had given 50 of the shares to his mother as a birthday present. How are we to tell whether he gave away trust shares or his own, unless we first know which of the 950 shares were held in trust? The problem is not solved, as Professor Martin maintains (Chapter 3: ‘Requirements of a trust’, Section 3 ‘Certainty’, Part B ‘Certainty of subject-matter’), by applying the rule of tracing (Chapter 19) that a trustee is presumed to use his own rights first, for that assumes the very thing we are trying to prove (i.e. that Moss was a trustee), when in fact the question being asked was whether or not he was a trustee. For a trenchant criticism, see Hayton (1994) 100 LQR 325; Oakley, Chapter 3: ‘The essential ingredients of a trust’.

The result in Hunter v Moss has been approved on the basis that the plaintiff’s declaration of 50 of his 950 shares for the defendant should create a trust of all 950 shares for both parties as tenants in common in the proportions of 50/950 for the defendant and 900/950 for the plaintiff. See Pearson v Lehman Brothers Finance SA [2010] EWHC 2914 (Ch) at [227]–[248]; affirmed [2011] EWCA Civ 1544 at [69]–[77]. Also see White v Shortall [2006] NSWSC 1379 starting at [148]; affirmed [2007] NSWCA 372.

5.2.3 ‘Future property’

It is not possible to create a trust of rights which the settlor does not currently have. Thus, I cannot today create a trust of the rights I expect to receive under my father’s will. A trustee holds rights for another, and if there are no rights, there can be no trust. Rights which I do not have yet but hope to have in the future are known as ‘future property’, which is not property even using the widest possible meaning of that term. It is of course possible to promise to settle (i.e. create a trust of) such rights if and when they are received, but that is something different again.

5.2.4 Consequences of inability to identify trust rights

This depends on whether we are dealing with a self-declaration of trust or a declaration accompanying a transfer. In the first case, nothing happens when a settlor fails to identify which rights are subject to their self-declared trust. Everything remains as before. Where there is a transfer, the position is more difficult. In Palmer v Simonds, the court held that the recipient took the rights outright. The thinking here is that uncertainty as to subject-matter feeds back into uncertainty as to intention to create a trust in the first place. This will not always be the case: Oakley, Chapter 3: ‘The essential ingredients of a trust’, Section I ‘The three certainties’, sub-part (A) ‘The property subject to the trust’.
ESSENTIAL READING

At least one of the following:


FURTHER READING

- Hayton & Mitchell, Chapter 4: ‘The three certainties’, Section 3 ‘Certainty of subject-matter’.

ACTIVITY 5.2


a. On what grounds did the court distinguish Re London Wine?

b. Is that distinction valid for all possible cases?

c. What explanations have been put forward to cope with the problem of dealings by the ‘settlor’ with part of the bulk?

No feedback provided.

Summary

The subject matter of a trust can consist of virtually all types of rights. However, it must be possible to clearly identify what rights are subject to the trust otherwise the trust cannot function, as shown by Re London Wine and Re Goldcorp. ‘Conceptual uncertainty’ can mean there is no valid declaration of trust, as was seen in Palmer v Simmonds. However, where a court can determine an appropriate meaning of the terms in the trust, the declaration of trust will be valid, as Re Golay’s WT illustrates. Special attention must be given to Hunter v Moss. Despite Re London Wine, the Court of Appeal did not say that the declaration was invalid but instead distinguished intangibles (shares) from tangibles (wine). The case consequently raises practical difficulties which currently have not been resolved. A testator’s residuary estate is always certain. It is everything left after the satisfaction of specific legacies in the will. A trust of rights which the settlor does not at that moment have cannot be created.

5.3 Identifying the beneficiaries

5.3.1 A non-charitable trust must have beneficiaries

A trust must have beneficiaries, unless it is for a charitable purpose (see Chapter 10) or for one of the anomalous non-charitable purposes which are permitted in English law (see Section 11.4). This is said to be one of the most fundamental principles of trust law. In Re Endacott [1960] Ch 232, a testator left his residuary estate to the North Tawton Parish Council on trust ‘for the purpose of providing some useful memorial to myself’. The Court of Appeal held that the trust failed because the testator had not identified any person or group of persons who were to be the beneficiaries of the trust. Instead of a trust for persons, the testator had attempted to create a trust for a purpose, and, since the purpose was not charitable, that was not permitted. Lord Evershed MR said:

No principle perhaps has greater sanction or authority behind it than the general proposition that a trust by English law, not being a charitable trust, in order to be effective, must have ascertained or ascertainable beneficiaries.
We will return to the topic of non-charitable purpose trusts in Chapter 11, where you will see that some cases have departed from this rule.

5.3.2 The beneficiaries must be identified

It is not enough that a trust has beneficiaries. If the trustees are to perform their functions under the trust, it must be possible to know who those beneficiaries are. This is the requirement of certainty of objects. Note that the tests for certainty differ according to whether we are dealing with a fixed or a discretionary trust. To have a full understanding of this topic, you will need to know the requirements for certainty of objects in relation to something which is not a trust at all: a power of appointment (discussed in Chapter 3). The key to understanding the various tests for certainty is to appreciate that they are not arbitrary inventions of the judges. Instead, they arise from the nature of things. If they are not satisfied, the trust (or power) could not function. Note that problems of certainty of objects only arise where the settlor uses a generic term to describe the class (for example, my children, my relatives or my friends). Where the beneficiaries are individually named, no question of uncertainty of objects arises. The whereabouts of such individuals may be unknown, but that is not something which will cause the declaration to be adjudged invalid.

Fixed trusts

As you know, in a fixed trust the settlor decides in advance the share each beneficiary is to receive. An example would be a trust for ‘my children in equal shares’. The test for certainty of objects, sometimes called the ‘complete list’ test, is that the trustee must be able to determine the identity of all members of the class. The obvious reason for this is that unless the identity of all members can be known, the trustee cannot distribute a single penny, if the amount each is to receive depends upon first making a complete list of every member of the class.

Discretionary trusts

You also know that in a discretionary trust (sometimes confusingly called a ‘trust power’, but which you should not mistake for a ‘power of appointment’ or ‘mere power’) the trustee has a discretion to choose how to distribute the trust assets among the potential objects. Since the trustee is not required to distribute income or capital equally to all, the share each will receive is not contingent on the number of people in the class. There is therefore no need for the trustees to compile a complete list of all potential beneficiaries to make any distribution: McPhail v Doulton [1970] UKHL 1, [1971] AC 424. The trustees do, however, need to be able to tell whether a potential object is or is not a member of the class, for they (and the court) need to know whether the proposed distribution is within their powers. This test for certainty of objects is generally called the ‘is or is not’ or ‘any given postulant’ test. If, for example, I give my trustees a discretion to distribute income from a trust fund to ‘tall students of the University of London’, the test of validity is whether they are able to tell which students are tall and which are not, for otherwise they may stray outside the terms of their discretion and thereby commit a breach of trust. Since neither they nor the court can tell where ‘tall’ starts and ‘not tall’ ends, such a trust would fail for ‘conceptual’ uncertainty. It is different where we know what the defining term means but do not have enough evidence to determine whether a particular person is or is not a member of the class, sometimes called a case of ‘evidential uncertainty’: Re Baden’s Deed Trusts (No 2) [1972] EWCA Civ 10, [1973] Ch 9. There, the burden of proof is on the postulant, the person claiming to be in the class and if the person does not prove that they are, then they are not.

It is a difficult question whether conceptual uncertainty can be cured by a term in the trust which makes a third party the arbiter: compare Re Tuck’s ST [1978] Ch 49 with Re Wright’s WT (1981) commentary in (1999) 13 Trust Law International 48.
Powers of appointment

Powers of appointment (or ‘mere powers’) are not trusts in themselves, but are often used in trust instruments. They also raise issues of certainty of objects, since powers may be created in favour of classes of people described only in generic terms. Since there is no duty to appoint equally to all members of the class but merely to stay within the terms of the power, the same test for certainty of objects (the ‘is or is not’ test) applies to powers of appointment as to discretionary trusts: *Re Gulbenkian’s ST* [1968] UKHL 5, [1970] AC 508. Indeed, it was from the law on powers of appointment that the test was taken in *McPhail v Doulton*.

Gifts subject to conditions

These are not trusts either, but because they are often phrased in generic terms, they raise similar issues to discretionary trusts. The question here is whether the same requirement of certainty of object is required, or whether it is enough to say of a particular candidate that they are or are not a member of the class: *Re Barlow’s WT* [1979] 1 WLR 278; criticised by *Emery* (1982) 98 LQR 551.

5.3.3 Consequences of failure

A trust with no certain beneficiaries is no different from a trust that has no beneficiaries. Thus, an attempt to create a trust for a non-charitable purpose will be treated in exactly the same way as an attempt to create a trust for uncertain beneficiaries. For both cases, we must distinguish between a self-declaration of trust and a transfer to a third party on trust. In the former, nothing happens. If I declare myself a trustee of rights for the purpose of providing a useful memorial to my wife, I remain the outright holder of the rights in question. The same is true if I declare myself a trustee for my ‘tall friends’. If, however, I transfer the rights to a third party on those same terms, a resulting trust will arise, with the third party as the trustee and me as the beneficiary. This is discussed in Chapter 12.

Essential reading

At least one of the following:


Further reading

- Hayton & Mitchell, Chapter 4: ‘The three certainties’, Section 4 ‘Certainty of beneficiaries’.

Activities 5.3–5.5


5.3 How do the approaches of Megaw LJ and Sachs LJ differ on the question of certainty of objects? Try to formulate a set of objects which would be valid under one but void under the other.

5.4 Explain the difference between ‘conceptual uncertainty’ and ‘evidential uncertainty’.

Go to your study pack and read ‘Powers, trusts, and classes of objects’ by A. Grubb.
5.5 What is the effect of evidential uncertainty on (a) a fixed trust, (b) a discretionary trust, and (c) a power of appointment?

5.3.4 Certainty of beneficiary’s interests

Even though the rights which are to be held on trust and the objects of that trust are sufficiently identified, it may be that the settlor has not identified the shares in which the beneficiaries are entitled under the trust. This is not a problem for a discretionary trust, since that will be determined by the trustees themselves. However, it will be a problem in a fixed trust, as in Boyce v Boyce (1849) 6 Sim 476, 60 ER 959, where one of two beneficiaries was given the task of allocating assets between them but died without doing so. That was an unusual case. Normally, if a trust is silent on how assets are to be divided among a list or class of beneficiaries, they will hold them in equal shares. See Oakley, Chapter 3.

5.3.5 Workability

This requirement arises out of the abandonment of the ‘fixed list’ test and the adoption of the ‘is or is not’ test of certainty of objects for discretionary trusts and the consequent acceptance of the prima facie validity of conceptually certain classes as huge as ‘relatives of X’ or ‘all the inhabitants of Greater London’. The members of such classes cannot be surveyed one by one. It may be suggested that if there is a ‘core class’ of objects within the larger class to whom the trustees may primarily devote their survey of objects before making payments, then the trust will not be administratively unworkable, although no case has explicitly stated that the absence of a ‘core class’ is the basis for the finding of such unworkability. On the ‘core class’ view, ‘relatives of X’ is workable because a core class easily identifies itself, i.e. the close relatives of X as opposed to distant relatives. ‘Residents of Greater London’ is not workable, because there is no such core class. The problem is not size. ‘Relatives of X’ is a larger class than ‘Residents of Greater London’. (You may find this surprising, but in law ‘relative’ or ‘relation’ means descendent of a common ancestor, and so, counting back to more and more distant ancestors and then back down to living persons, everyone undoubtedly has many more relations than they could ever identify, and we are all related if we want to go as far back as the first humans to arise in Africa.) The problem is solely being able to identify a core class capable of being surveyed. In Re Manisty’s ST [1974] Ch 17, Templeman J associated the concept of administrative unworkability with ‘capriciousness’, saying that a power of appointment given to a fiduciary in favour of the ‘residents of Greater London’ was capricious because the terms of the power negated any sensible intention on the part of the settlor. However, in Re Hay’s ST [1981] 3 All ER 786, [1982] 1 WLR 202, Megarry J doubted that such a trust would be capricious if the settlor had been a former Chairman of the Greater London Council (and in such a case the power, though valid, would equally disclose no ‘core class’).

ESSENTIAL READING

At least one of the following:


FURTHER READING

- Hayton & Mitchell, Chapter 4: ‘The three certainties’, Section 4 ‘Certainty of beneficiaries’.

Go to your study pack and read ‘A heresy and a half in certainty of objects’ by P. Matthews.
Activity 5.6

a. Within powers of appointment, why does it matter whether the power is held by a fiduciary?

b. On what basis does Megarry J suggest that ‘intermediate’ trusts are administratively unworkable?

Summary
A fundamental principle of trust law is that a trust must have beneficiaries. However, this is not sufficient, and there must also be ‘certainty of objects’. This problem potentially arises when a generic term is used to describe a class. The criterion for ‘certainty of objects’ differs depending on whether it is a fixed trust, on the one hand, or a discretionary trust or power of appointment, on the other. In a fixed trust, a trustee must be able to compile a complete list of the beneficiaries, while in the case of a discretionary trust or power of appointment the trustee must be able to determine whether any given postulant is or is not a member of the class.

Apart from charitable trusts and a few anomalous exceptions, a trust cannot exist if it has no beneficiaries or the beneficiaries cannot be identified with certainty. Where the intended trust is self-declared, the invalid declaration of trust will mean that nothing has happened, and the would-be settlor will simply retain the rights concerned for himself. Where the would-be settlor transfers rights to a would-be trustee and the declaration is invalid for failure to identify the objects, the would-be trustee holds them on resulting trust for the would-be settlor.

The requirement of administrative workability is unclear, though it may be given content by regarding the absence of a core class as rendering a trust administratively unworkable.

5.3.6 Perpetuity

Essential reading

This subject is not examinable, but its understanding will help you to appreciate why perpetuity can sometimes be problematic. Basically, the rule against perpetuities prevents settlors creating perpetual trusts. At some point, the beneficiaries must be free to wind up the trust and call for a transfer of the rights to them. Before the introduction of legislation in 1964, a trust that violated the common law rule against perpetuities was void from the outset. Now, under the Perpetuities and Accumulations Act 2009, a trust that might violate the rule is valid for up to 125 years. There are exceptions (in s.2) for charitable trusts and pension schemes, to which no perpetuity period applies. The Lord Chancellor has the power (under s.3) to specify other exemptions.

Sample examination questions

Question 1 Advise on the validity of the following provisions in Martin’s will:

a. £50,000 to my executors in trust for distribution amongst such loyal supporters of Manchester United Football Club as my executors think fit. In the event that there is a dispute as to whether any given person is a loyal supporter, the current captain of Manchester United to decide.

b. £50,000 to my executors on trust for distribution amongst such members of the Manchester United Supporters Club who are over six feet tall as my executor thinks fit.

c. £500,000 to my executors for distribution in equal shares amongst all persons listed in the Manchester telephone directory whose surnames begin with Z.

d. My collection of Manchester United football programmes to be available for purchase at £1 each to any friends who travelled with me to matches.
Question 2  Nigel has recently died. A week prior to his death, he declared in writing that he held 200 shares in Oilco plc on trust for Martin. At that point, Nigel held 1,000 shares in Oilco plc outright. By his will, Nigel left his residuary estate to his widow 'in the confident expectation that she will use it for the benefit of our children'.

Advise Nigel’s children.

ADVICE ON ANSWERING THE QUESTIONS

Question 1  This question raises issues of certainty of objects and administrative workability in relation to trusts and gifts. Each part will be addressed in turn:

a.  This is an attempt to create a discretionary trust, the objects of which are the 'loyal supporters of Manchester United Football Club'. The question is whether the class is defined with sufficient certainty. The answer should outline the content of that test, noting the different formulations of Megaw and Sachs JJ in Re Baden (No 2). They should then apply those formulations to the facts of the case before them. A further question is whether, should the class be too uncertain, that uncertainty can be cured by the provision that the team captain is to decide on membership.

b.  This is again a discretionary trust, though with the difference that there is no uncertainty as to whether any given individual is or is not a member of the benefited class. The issue instead is one of administrative workability or capriciousness, the class as defined seeming to be an arbitrary collection of individuals.

c.  This is a fixed trust, where the test for certainty of objects is different. Candidates should state what that test is and whether it is satisfied in this case. There is then a question whether a requirement of administrative workability can apply in a case such as this.

d.  This is not a trust but a gift subject to a condition precedent, to which Browne-Wilkinson J in Re Barlow’s WT held that a less stringent test that the 'is or is not' test applied. Note, however, the trenchant criticism of this decision by Emery (1982) 98 LQR 551, 562–67.

Question 2  There are two issues which need to be discussed: the inter vivos declaration of trust in favour of Martin and the testamentary transfer to Nigel’s widow. The children will want to argue first that the inter vivos declaration of trust was of no effect, with the result that all 1,000 shares form part of Nigel’s residuary estate. They will also want to argue that the transfer of the residuary estate to their mother was a transfer to her on trust for them rather than outright.

As to the first issue, though there is clearly an intent to create a trust and the identification of a beneficiary, the problematic area is that of the subject-matter of the trust: Nigel has 1,000 shares and we do not know which of those share are subject to the trust and which are not. While there is no doubt that such a problem would be fatal were we talking about rights to tangible things (e.g. bottles of wine: Re London Wine), the question is whether a different rule should apply to the case of shares. The discussion should therefore point out the differences between shares and wine and go on to discuss the case of Hunter v Moss. The question is essentially asking whether Hunter v Moss was correctly decided, so you will need to know not only what the Court of Appeal held but also the academic criticisms (and defence) of that case.

The second issue raises questions of certainty of intention to create a trust. The question is whether the words used by the testator (‘in the confident expectation that she will use it for our children’s benefit’) are sufficiently mandatory to create a trust or, as in Re Adams & Kensington Vestry, simply express a preference by the testator as to what the recipient should do with the rights. Note that there is no problem over certainty of subject-matter with the gift of the residuary estate.
**Reflect and review**

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th></th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can explain how</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>the court</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>determines</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>whether the</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>words expressed</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>by a person</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>showed an intention to create a trust.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can define the test for certainty of subject-matter of a trust.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain why the tests for certainty of objects</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>differ between fixed trusts, discretionary trusts, and powers of appointment.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain the concept of administrative workability.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.1 Intention to create a trust</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.2 Identifying the rights</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.3 Identifying the beneficiaries</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
6 Creating express trusts II: constitution

Contents

Introduction ................................................................. 62
6.1 Constituting a trust .................................................. 63
6.2 Defective constitution .............................................. 64
Reflect and review ...................................................... 69
Introduction

This chapter is concerned with the constitution of express trusts, by which is meant the vesting in the intended trustees of the rights that will form the subject-matter of the trust. There are three issues to discuss. First, how is a trust constituted? Second, what will the court do if the constitution is in some way defective? Third, because the same rules as to constitution also apply to the making of gifts, we need also ask what equity does about defective gifts and unperformed promises to make gifts. Strictly speaking, this is a diversion, for when the courts do intervene, they do so by the imposition of trusts on the right-holder. Since these trusts will be constructive rather than express, the topic properly forms part of Chapters 18 and 19. It is dealt with here for reasons of convenience. A related topic is that of unperformed promises to create trusts. These are dealt with in Chapter 9.

Essential reading


Learning outcomes

By the end of this chapter and the relevant reading, you should be able to:

- identify the different ways in which a trust can be constituted
- describe and analyse the situations in which a court may make perfect a defective gift.
6.1 Constituting a trust

6.1.1 The requirement of perfect constitution

A trust will be perfectly constituted where the rights in question are vested in the intended trustees. This involves a transfer of those rights to the trustees. Where the settlor himself is to be the sole trustee, then no transfer is required. There are therefore never issues of constitution in such cases. As discussed in the previous chapter, where the settlor is one of several intended trustees, the settlor as trustee will come under an enforceable trust duty to transfer the trust assets into the joint names of all the trustees, so there is a mechanism to achieve proper constitution: *T Choithram International SA v Pagarani* [2000] UKPC 46, [2001] 1 WLR 1, [2001] 2 All ER 492.

Assume, therefore, that we are dealing with the (more usual) case of a settlor who wants other people to act as the trustees. How that settlor manages to pass the right to the trustees depends on the nature of the right itself.

- For title to land, the trustees will need to become the registered proprietors of the title. This requires execution of a deed in the proper form and its registration at the Land Registry. If the land is unregistered, then the transfer will trigger compulsory registration under the Land Registration Act 2002.

- For title to tangible chattels (including goods, documents, and cash), it will have to be conveyed by deed or delivery (i.e. a physical handing over of the thing).

- For a chose in action (e.g. a right to sue on a debt or a share) then the rules differ as between the different types of choses in action. Shares in a private company can only be transferred by the making of an entry in the company’s books by the company secretary. In the case of public companies traded on stock exchanges, there are now computer-automated systems for the transfer of shares. A debt can only be transferred at law by a written instrument.

- For equitable interests, such as interests under trusts or equitable charges, these normally must be assigned in writing signed by the assignor: s.53(1)(c) LPA 1925.

It should be stressed that these methods describe the ways in which the relevant rights need to be transferred to the intended trustees. They do not apply to self-declarations of trust, for which a transfer is not required. Students often assume they do, but you should not make that mistake.

It is also important to note that constitution is not normally a problem for testamentary trusts, which are created by the settlor’s will. When the settlor dies, their assets will be transferred by operation of law to the executors or administrators of the estate. They have a duty to administer the estate, including the constitution of any trusts set out in the will. In many cases, the executors will also be the trustees of those trusts and so will already have title to the trust assets when administration is complete and the trusts take effect. A problem can arise if there are insufficient assets in the estate, because the estate debts must be paid first. All or some of the assets that were supposed to be settled in trust might have to be used to pay those debts.

The methods described above are also those which need to be used to make outright gifts of the various types of right.

6.1.2 The effect of perfect constitution

Once a trust is perfectly constituted, the beneficiaries of that trust can enforce it against the trustees, whether or not they have given value to anyone in exchange for its creation. Like an outright gift, a settlor cannot revoke a perfectly constituted trust on the ground that the beneficiaries gave nothing in return. It matters not in the case of a perfectly constituted trust that the beneficiaries are volunteers (i.e. donees). The point only becomes contentious where there is some defect of constitution.


**Essential Reading**

At least one of the following:

- Martin, Chapter 4: ‘Constitution of trusts: equity will not assist a volunteer’.
- Oakley, Chapter 5: ‘The constitution of a trust’, paras 5-001–5-019.
- Pettit, Chapter 6: ‘Completely and incompletely constituted trusts’, Section 1 ‘The perfect creation of a trust’.
- Cases: *Milroy v Lord* (1862) 4 De GP & J 264, 45 ER 1185; *Paul v Paul* (1882) 20 Ch D 742.

**Further Reading**


### 6.2 Defective constitution

#### 6.2.1 The general rule

The general rule, set out in *Milroy v Lord*, is that equity will not assist a volunteer to perfect an imperfect trust. This is consistent with the general attitude of both the common law and equity to the enforcement of gratuitous promises which you saw when studying the law of contract. Consistently with this approach, *Milroy v Lord* further holds that an imperfect attempt to create a trust with other persons as trustees will not be interpreted as a declaration by the settlor of themself as trustee. As the court there pointed out, an intention to constitute others as trustees is inconsistent with any argument that the settlor intended to make themself a trustee.

Exactly the same thinking means that a donor who tried but failed to make an outright gift will not be seen as having declared himself a trustee: *Richards v Delbridge* (1874) LR 18 Eq 11. As was pointed out in *Milroy v Lord*, if that were possible, there would be no such thing as an imperfect gift.

#### 6.2.2 Departures from the general rule

As we have seen, the general rule is that if the settlor has not managed to create a perfect trust, the courts will not intervene to create one for him. Any intervention by the court, as *Milroy v Lord* and *Richards v Delbridge* demonstrate, would be to create a trust that was not intended by the settlor or donor. In other words, it would produce a constructive trust. We will see immediately below that the courts do sometimes intervene and impose a trust on the purported donor in favour of the donee. Indeed, there are six situations in which courts have departed from the rule in *Milroy v Lord*. It should be asked whether all these departures are justified.

**Activity 6.1**

What limits does *Milroy v Lord* place on what (a)settlers and (b) the courts can do in respect of constituting a trust?

1. Detrimental reliance

Where there is an imperfect gift or trust, there may be detrimental reliance on the part of the intended donee/beneficiary. For example, the intended donee of a gift of a title to land detrimentally rely on the supposed validity of the transfer by expending money building a house on that land. Detrimental reliance may lead the court to order the perfection of the imperfect gift or trust: *Dillwyn v Llewelyn* (1862) 4 De GF&J 517; *Pascoe v Turner* [1978] EWCA Civ 2; *Thorner v Major* [2009] UKHL 18. If so, the purported transferor will hold the promised right on constructive trust for the intended donee. This process is usually called ‘proprietary estoppel’ (which is similar to, but different from, ‘promissory estoppel’ studied in the law of contract). It might be asked why the law does not simply respond by forcing the ineffective donor to pay compensation for the donee’s loss rather than making good the donee’s expectation.
2. The rule in Re Rose

Where a donor or settlor requires the assistance of a third party to perfect a gift or trust (which happens in cases where the transfer must be completed by registration of title, either to land or to shares in a private company), there will be a gap between the time at which the donor does everything within their power to perfect the gift or trust (i.e. fills in and provides the donee with the relevant transfer request forms) and the time when it is actually perfected by the change of the entry in the register. The question that arose in *Re Rose* [1952] EWCA Civ 4 was whether an intended gift and trust could be said to be perfect at the first stage. The Court of Appeal held that the donor/settlor was a constructive trustee of the rights at this point. The reason, said the court, was to be found in notions of ‘common sense’, which, of course, is no reason at all. Note that there was no detrimental reliance in this case nor (as some students insist) can it be explained by an application of the magic formula that ‘equity looks upon that as done which ought to be done’, for there was no ‘ought’ here. There is no duty in English law to make gifts.

3. The rule in *Strong v Bird*

At common law, the appointment of a debtor to be the creditor’s executor erased the debt, on the ground that it was not possible for the executor to sue himself to recover it. Equity very soon intervened to correct what was seen to be an unjust rule and held that a liability still existed in equity. In *Strong v Bird* (1874) LR 18 Eq 315 the testatrix had purported to release the debt during her lifetime. That release was ineffective since it was not made by deed, so it was nothing more than a bare promise not to sue. However, because there was an intention to relieve the debt and that intention continued until the testatrix’s death, the court refused to intervene in its usual manner. Technically, this might not be seen as the court perfecting an imperfect gift, for all it did was decline to interfere with the common law position. However, later cases extended the rule beyond the release of debts to imperfect transfers of all types of rights: see *Re Stewart* [1908] 2 Ch 251. It has even been used in the case of imperfect *inter vivos* gifts to administrators: *Re James* [1935] Ch 449. Once again, there is no requirement of detrimental reliance.

4. The rule in *Re Ralli*

This looks similar to the rule in *Strong v Bird*, but seems to form a separate rule (if that is what it is, since it was only an obiter pronouncement in a first instance case), because it applies even though there is no continuing evidence of an intention to give. Indeed, given that it involved an unperformed promise to give rather than a failed donation, any talk of a continuing intention is nonsense. In *Re Ralli* [1964] Ch 288, a promise by deed (covenant) to create a trust had not been performed during the lifetime of the promisor. The promisee was appointed executor of the promisor’s will, and on the latter’s death, received the promised rights by virtue of that office. Buckley J held, obiter, that this was enough to constitute the covenanted for trust. The fact that the executor came by the right fortuitously was irrelevant. The decision is difficult to square with the earlier decision of *Re Brook’s ST* [1939] Ch 993, which was not cited to the judge.

5. *Donatio mortis causa*

A *donatio mortis causa* is a gift which is made in contemplation of the donor’s death and is conditional upon their death. A typical case is where I hand you my watch and tell you that, if I do not survive the dangerous operation I am about to undergo, the watch is yours to keep. In *Re Beaumont* [1902] 1 Ch 889, 892, Buckley J said: ‘A *donatio mortis causa* is a singular form of gift. It may be said to be of an amphibious nature, being a gift which is neither entirely *inter vivos* nor testamentary.’ It does not have to satisfy the normal requirements for making either form of gift. It is sufficient if the donee merely acquires control over the intended gift so that the donor can no longer deal with it freely. If the donee does not obtain legal title by delivery, the donor’s executors or administrators will hold title on constructive trust for the donee: *Duffield v Elwes (Hicks)* (1827) 1 Bli NS 497; *Sen v Headley* [1991] EWCA Civ 13. The conditions for the operation of the rule are laid down in *Cain v Moon* [1896] 2 QB 283.
6. Unconscionability

A further dilution of the *Milroy v Lord* principle occurred in *Pennington v Waine* [2002] EWCA Civ 227, where the Court of Appeal said of an imperfect gift of shares, that the donor need not even have done everything necessary to perfect the gift. What mattered instead was whether it would be 'unconscionable' for her to resile from her gift. On the facts of this particular case, it was said to be 'unconscionable' for the donor to resile as she had told the donee that the gift was perfect. Why this makes it 'unconscionable' was not explained: see *Zeital v Kaye* [2010] Civ 159, [40]. Moreover, no member of the court seems to have noticed that this is precisely what happened in *Milroy v Lord*. The court relied on *T Choithram v Pagarani Int SA* [2000] UKPC 46 as authority, though that was, as we saw in the previous chapter, a case of an express trust, where it would of course be 'unconscionable' to resile from a perfectly valid trust: see *Paul v Paul*, *Pennington v Waine*, on the other hand, was a case of a constructive trust, for whichever way one views it, the purported donor did not make a self-declaration of trust. It is also important to note that the result cannot be defended through an application of the dubious doctrine in *Re Rose*, since the donor had not done all she needed to perfect the gift, nor can it be justified on the basis of detrimental reliance on the part of the purported donee. Although such reliance was arguably present, this was not the basis on which the case was reasoned.

**Essential Reading**

At least one of the following:

- Martin, Chapter 4: 'Constitution of trusts. Equity will not assist a volunteer', Section 2 'Transfer of the property to trustees upon trust' and Section 7 'Exceptions to the rule that equity will not assist a volunteer'.
- Oakley, Chapter 5: 'The constitution of a trust', Section II 'When will a trust be completely constituted?' Parts 3 and 4.
- Pettit, Chapter 6: 'Completely and incompletely constituted trusts', Section 1 'The perfect creation of a trust' and Section 6 'Exceptions to the maxim that “equity will not assist a volunteer”'.

**Cases:**


**Further Reading**

- Hayton & Mitchell, Chapter 2: 'Constitution of trusts'.

**Self-assessment questions**

1. When is a trust constituted?
2. What are the 'constitution' requirements in the case of a self-declaration of trust?
3. What means must be used to transfer the following to a third-party trustee:
   a. title to land
   b. shares in a private company
   c. the benefit of a debt.
4. What is the general rule contained in *Milroy v Lord*?
5. What is a donatio mortis causa?

6. What is the closest that English law comes to the continental European notion of a ‘foundation’?

7. What is a ‘perfect’ gift?

**Activity 6.2**

a. Assume that you want to make a gift of some shares and your title to a painting to a friend. Give a short spoken explanation of the different ways in which that gift can be made. Which is the simplest to effect?

b. Read the decision of the Court of Appeal in Re Rose. Is it really true that it presents no conflict with the same court’s earlier decision in Milroy v Lord?

c. Does the law in this area teach us anything of the meaning of ‘unconscionability’?

**Summary**

‘Equity will not assist a volunteer to perfect an imperfect trust’ is the general rule contained in Milroy v Lord. However, it has been shown that the courts have departed from this rule and intervened in six situations:

- detrimental reliance
- the rule in Re Rose
- the rule in Strong v Bird
- the ‘rule’ in Re Ralli
- donatio mortis causa
- unconscionability.

The effect of the courts’ intervention has been to effectively confer an intended right on a donee despite the donor failing to comply with the necessary legal requirements. In each case, one should question whether these interventions can be justified, first, as a matter of principle, and second, in light of the general rule laid down in Milroy v Lord.

**Sample examination questions**

**Question 1** How far is it true to say that equity will not perfect imperfect gifts?

**Question 2** Sarah owns 500 shares in a private company. She executes an instrument of transfer of the shares in the form required by the company’s Articles, and hands it, together with the share certificates, to Daphne, to whom she has promised them as a gift. Sarah dies before the share transfers are registered by the company.

By her will, Sarah appoints Bernard her executor, leaving all her real and personal property to Jacob who, immediately on her death, cancels the instrument of transfer.

Advise Daphne. How, if at all, would your answer differ if Daphne rather than Bernard had been appointed Sarah’s executor?

**Advice on answering the questions**

**Question 1** A good answer would start by outlining what is meant by a perfect gift, explaining that there are effectively three methods of giving, either through an outright transfer, a transfer on trust, or a self-declaration of trust. It would then explain that the possibility of an imperfect gift only arises in the first two cases, and that the imperfection would be caused by an ineffective attempt to transfer the right which is to form the subject-matter of the gift or trust. No question of an imperfect gift could arise in the case of the third method, for no transfer of any rights is necessary.

The next question is whether a court will intervene to force the perfection of the imperfect gift by imposing a trust on the donor of the rights in question for the
putative donee/beneficiary. The answer given by the Court of Appeal in Milroy v Lord and Richards v Delbridge was that it would not. Nor would it reinterpret what had happened as a self-declaration of trust by the donor/settlor, for in neither case had the donor/settlor ever made a self-declaration of trust. Indeed, the evidence of the failed gift contradicts such an interpretation of events.

Having stated the general rule, the answer would go on to detail the situations in which departures from this rule have been made. A good answer would notice that in only one instance is any detrimental reliance required, and ask how those in which it is not can be squared with the rule that courts will not assist volunteers to perfect imperfect gifts.

**Question 2** A good answer would start by explaining why this gift is problematic and explaining what steps Sarah should have taken to perfect it. The answer would outline the general rule in Milroy v Lord (as per Question 1), noting that the facts here might fall within the exception in Re Rose. In that respect, there are essentially two issues to consider: (i) whether on these facts the rule in Re Rose will apply, and (ii) if so, whether the rule is open to challenge. Finally, the answer should consider the application of the rule in Strong v Bird in the event that Daphne is appointed executor.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th></th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can identify the different ways in which a trust can be constituted.</td>
<td>□</td>
<td>□</td>
<td>□</td>
</tr>
<tr>
<td>I can describe and analyse the situations in which a court may make perfect a defective gift.</td>
<td>□</td>
<td>□</td>
<td>□</td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>6.1 Constituting a trust</td>
<td>□</td>
<td>□</td>
</tr>
<tr>
<td>6.2 Defective constitution</td>
<td>□</td>
<td>□</td>
</tr>
</tbody>
</table>
7 Proving declarations of trust and effecting dispositions of a beneficiary’s interest under a trust

Contents

Introduction ................................................. 72
7.1 Proving a declaration of trust ............................. 73
7.2 Transfer of equitable interests ............................. 76
Reflect and review ........................................... 80
Introduction

This chapter is concerned with two separate questions. First, what type of evidence is admissible in court to substantiate an allegation that someone has made a declaration of trust? This issue also arises in the context of testamentary trusts, and is discussed in the next chapter (Chapter 8: ‘Secret trusts’). Second, how does a beneficiary of a trust transfer their interest? These two topics bear no relation to each other, save that the rules governing both are stated in the same sub-section of a statute. Experience, however, shows that students (and some judges) are prone to confuse them, so you should ensure that, despite their proximity, both in legislation and in the textbooks, you do not fall into that trap.

Essential reading

- Penner, Chapter 6: ‘Formalities and secret trusts’, paras 6.1–6.42.

Learning outcomes

By the end of this chapter and the relevant reading, you will be able to:

- identify the difference between substantive requirements of a declaration of trust and procedural rules relating to its proof
- describe the origin and nature of these procedural rules
- identify the substantive rules relating to how dispositions of interests under trusts are made.
7.1 Proving a declaration of trust

In truth, this topic is part of the law of evidence. One issue in the law of evidence is the type of evidence admissible in court to prove the truth of allegations of the occurrence of events. To take just one example, the law of evidence decrees that hearsay evidence – testimony of one person as to what another person is supposed to have said – is admissible to prove events alleged to have occurred in civil proceedings but generally not in criminal proceedings. The type of evidence we are concerned with here is oral testimony. Generally speaking, oral testimony is admissible in civil cases to prove the truth of an allegation that a particular event occurred. For example, you will have seen when you studied the law of contract that there is generally no restriction on the types of evidence which the court will admit to prove that a contract had been made. So too as to whether a tort was committed.

The same general rule applies to allegations that a right-holder has made a declaration of trust. In general, as you will have seen from your reading of Paul v Constance in Chapter 5, there is no objection to oral evidence being admitted to make good such an allegation. There are, however, two exceptions to this rule. The first, which is dealt with in this chapter, concerns declarations of trusts of land. The second, addressed in the next, concerns testamentary trusts.

7.1.1 The admissibility rule

Statute provides that declarations of trust regarding land must be ‘manifested and proved’ by some writing. The rule is an ancient one, s.7 of the Statute of Frauds 1677 providing that:

... all declarations or creations of trust or confidences of any lands, tenements or hereditaments shall be manifested and proved by some writing signed by the party who is by law enabled to declare such trust, or by his last will in writing, or else they shall be utterly void and of none effect.

That section was re-enacted as s.53(1)(b) of the LPA 1925 as follows:

a declaration of trust respecting any land or any interest therein must be manifested and proved by some writing signed by some person who is able to declare such trust or by his will.

The reason for the enactment of s.7 in 1677 was, as the name of the statute implies, to prevent fraud. To understand how it and its successor operate, we must determine the fraud it was trying to prevent. Details of this can be found in the article by Youdan referred to below. Very briefly, the problem at that time was perjury, the giving of false evidence in court proceedings. The law of evidence in 1677 was in a primitive state, and it was consequently easy for fraudulent allegations to be made good in court. The fraudulent allegation in question was that the holder of title to land had declared himself a trustee of his title for the claimant. The title-holder, of course, had done no such thing, but because of the then primitive state of the law of evidence, the court would often find as a fact that such a declaration had been made and as a consequence order the title-holder to convey their title to the claimant. By this method, many title-holders effectively had their titles stolen from them. To put a stop to this abuse, the legislature provided that fraudulent allegations of self-declaration of trust were now less likely to succeed.

Note that the statute says nothing about the time when the written evidence must come into being. It is therefore no objection that it antedates or postdates the declaration of trust itself. Thus, it is perfectly possible to adduce written evidence which came into being today to prove a declaration of trust made a year ago. This is in stark contrast to the writing requirements which concern dispositions of equitable interests under trusts, which are not procedural but substantive. Nor, as some judges will tell you (for example, Lord Diplock in Gissing v Gissing [1970] UKHL 3) does the statute provide that the declaration itself be ‘in’ writing. This is an important point to grasp, for it is probably the most common mistake that students make in this area.
7.1.2 Effect of oral declaration

Since s.53(1)(b) of the LPA 1925 only states a rule of evidence, an oral declaration of trust can be valid. The problem will come in litigation if it is denied that such a declaration was made and there is no evidence sanctioned by the statute to prove that controverted fact.

It is often said of such a case that there is a 'valid but unenforceable' trust. This is unfortunate, and seemingly based on a false analogy with the old rule on contracts for the sale of interests in land (see, for example, Scott, A.W. [1955] ‘Construction trusts’ 71 LQR 39, 43). Section 40(1) of the LPA 1925, a provision repealed in 1989, used to provide that:

No action may be brought upon any contract for the sale or other disposition of land or any interest in land, unless the agreement upon which such action is brought, or some memorandum or note thereof, is in writing, and signed by the party to be charged or by some person thereunto by him lawfully authorised.

Under this provision, the lack of a written memorandum or note thereof did not render the contract void, merely unenforceable by court action. The contract was perfectly valid, and its existence could be proved by oral evidence. The only prohibition was on its enforcement. Section 53(1)(b), by contrast, is not concerned with enforceability but with proof, a logically prior question. If a declaration of trust is alleged to have been made but an application of the statute means that that allegation cannot be made good, there will in the eye of the court be no trust at all, not a valid but unenforceable one.

7.1.3 Exceptions to the rule

The difficulty with a statute which excludes evidence because it is not of a particular type is that it necessarily excludes both genuine and false evidence. It might be thought that that was a price worth paying. It has, however, caused the courts to pause, and in certain circumstances they have been ready to admit evidence which the statute says they cannot. The leading case is Rochefoucauld v Boustead [1897] 1 Ch 196, where the Court of Appeal held that a statute designed to prevent fraud could not be used to perpetrate a fraud, and therefore admitted oral evidence to substantiate an allegation of a declaration of trust on the ground that the ‘trustee’ himself would commit a fraud if he were allowed to shelter behind the statutory provision and deny the declaration of trust. Similar reasoning occurs in relation to secret trusts (Chapter 8). You should ask whether the reasoning in Rochefoucauld is not circular. It will only be a fraud if the defendant is a trustee, but at the point where the argument over admissibility is made, we do not yet have evidence showing that the defendant is a trustee.

7.1.4 The type of trust enforced in Rochefoucauld

What type of trust is enforced in a case such as Rochefoucauld v Boustead? Logically, it must be an express trust, for the event which triggers the finding that a trust exists is the now proved by evidence of a declaration of trust. Indeed, this is exactly what the Court of Appeal held (as part of the ratio of the case). Other cases, however, have called it constructive (Bannister v Bannister [1948] 2 All ER 133; Paragon Finance v Thakarer [1998] EWCA Civ 1249; [1999] 1 All ER 400). However, as we saw in Chapter 3, a constructive trust normally arises for some reason other than a declaration of trust on the part of a right-holder. The Rochefoucauld trust, by contrast, arose because of proof by evidence of a declaration of trust.

7.1.5 A statutory exception to the formality requirement

Section 7 of the Statute of Frauds was qualified by s.8, which read as follows:

Provided always, that where any conveyance shall be made of any lands or tenements by which a trust or confidence shall or may arise or result by the implication or construction of law, or be transferred or extinguished by an act or operation of law, then and in every
Section 8 was re-enacted as the much shorter s.53(2) of the LPA 1925:

This section does not affect the creation or operation of resulting, implied or constructive trusts.

The subsection merely states the obvious. Given that s.53(1)(b) is concerned with questions of the type of evidence admissible to prove that a declaration of trust was made, it makes perfect sense to exclude from its operation those trusts which, for one reason or another, do not require proof by evidence of a declaration of trust.

7.1.6 The matrimonial homes cases

There are a group of cases, the most of prominent of which are Pettitt v Pettitt [1970] UKHL 3, Gissing v Gissing [1969] UKHL 5, Lloyds Bank plc v Rosset [1990] UKHL 4, Stack v Dowden [2007] UKHL 17, and Jones v Kernott [2011] UKSC 53, which concern attempts to say there is a trust of the ‘matrimonial home’. Such cases usually run into problems with, among other things, s.53(1)(b) of the LPA 1925. Such trusts are therein called ‘constructive trusts’, and more specifically, ‘common intention constructive trusts’. Given that a constructive trust is one which normally arises for a reason other than of a declaration of trust by a right-holder, it may seem that the idea of a constructive trust based on an intention to create a trust is something of a misnomer. However, as Professor Birks famously said in *An introduction to the law of restitution* (Oxford: Clarendon Press, 1985) p.65:

There is a fine but important distinction between intent conceived as creative of rights, as in an express trust or a contract, and intent conceived as a fact which, along with others, calls for the creation of rights by operation of law.

The matrimonial home cases can be understood as cases in which the intention to share the property is not sufficient on its own to create an express trust, but is a fact that calls for the imposition of a constructive trust when there have been sufficient acts of detrimental reliance on that intention. This is similar to proprietary estoppel (discussed briefly in the previous chapter) and was clearly the approach taken in *Lloyds Bank plc v Rosset*, where Lord Bridge said:

Once a finding [of an agreement or arrangement to share] is made it will only be necessary for the partner asserting a claim to a beneficial interest against the partner entitled to the legal estate to show that he or she has acted to his or her detriment or significantly altered his or her position in reliance on the agreement in order to give rise to a constructive trust or a proprietary estoppel.

However, more recently in *Jones v Kernott*, the Supreme Court made no mention of detrimental reliance nor did it provide any explanation why an unexpressed intention to share a home can give rise to a trust without having to comply with s.53(1)(b) of the LPA 1925.

**ESSENTIAL READING**

At least one of the following:

- Martin, Chapter 3: ‘Requirements of a trust’, Section 2 ‘Formalities’.
- Oakley, Chapter 4: ‘The formal requirements for the creation of a trust’, Section II ‘The statutory requirement of writing’.
- Pettit, Chapter 5: ‘Formal requirements of express trusts’, Section 1 ‘Inter vivos transactions’.
Further reading


Activity 7.1

Read and note the decision in Gissing v Gissing.

a. What does the House of Lords say about the courts’ ability to create trusts in the absence of a declaration of trust by the right-holder?

b. If the right-holder in such a case did declare a trust, what problem would stand in the way of its proof?

c. What, for Lord Diplock, is the purpose of detrimental reliance in such a case?

d. How does Lord Diplock categorise the trust which would be consequently enforced? Is he correct to do so? Why do you think he classifies it so?

No feedback provided.

7.2 Transfer of equitable interests

The beneficiary of a fixed trust has an interest which is capable of assignment (transfer) to others. So far as courts of equity were concerned, this could be done orally. However, statutory rules have long said that only written assignments are effective. The original provision was s.9 of the Statute of Frauds 1677, which provided that:

... all grants and assignments of any trust or confidence shall likewise be in writing, signed by the party granting or assigning the same or by such law will or devise, or else shall likewise be utterly void and of none effect.

The current rule is contained in s.53(1)(c) of the LPA 1925:

a disposition of an equitable interest or trust subsisting at the time of the disposition must be in writing signed by the person disposing of the same or by his agent thereunto lawfully authorised in writing or by will.

While we saw that s.53(1)(b) of the LPA 1925 is evidential, s.53(1)(c) has been treated by the courts as dispositive. It is, in other words, a rule of substantive law, not procedure. What this means is that there is no question of an unwritten disposition being valid in the absence of litigation disputing its occurrence. There will instead, as Grey v IRC [1959] UKHL 2 demonstrates, be no disposition until the writing is executed. It might be asked whether, given the similarity in wording between ss.7 and 9 of the Statute of Frauds 1677, there should be this fundamental difference between the two provisions. However, this is the approach the courts have taken and to understand this area of law, that fundamental difference must never be forgotten.

7.2.1 What transactions are caught?

This all depends on what is considered a ‘disposition’. The leading case is Grey v IRC. Although the 1677 statute talked only of ‘assignments’, the House of Lords in Grey held that the two were not to be equated, and that the word ‘disposition’, though it included assignments, had a wider meaning. For that reason, a direction by a beneficiary to his trustees to hold the rights on trust for a third party, though it might not have been caught by s.9, was held to be covered by s.53(1)(c), with the result that there was no effective disposal by the beneficiary of his interest under the trust until he put his direction in writing. Other transactions which you need to consider are a direction by the beneficiary to the trustee to assign the right to a third party (Vandervell v IRC [1966] UKHL 3), a self-declaration of trust by the beneficiary (Grainge v Wilberforce (1889) 5 TLR 436), a declaration of trust by the trustee for a third party with...
7.2.2 Is s.53(1)(c) confined to trusts of land?

It will have already been seen that s.53(1)(b) of the LPA 1925 applies only to the case where there is an allegation that a declaration of trust has occurred in respect of an interest in land. The question is whether the same goes for s.53(1)(c). It is assumed in all the leading cases (Grey, Oughtred, and Vandervell) that it is not so restricted, and that trusts of all rights, not just property rights in respect of land, are caught. Opinion on the same question with regard to s.9 of the Statute of Frauds 1677 was divided and it is noteworthy that s.205(x) of the LPA 1925 defines ‘equitable interests’ as ‘equitable interests … in or over land or in the proceeds of sale thereof’. There is an argument, therefore, that the leading cases in this area, Grey, Oughtred and Vandervell, were decided per incuriam this statutory provision.

7.2.3 The rationale of s.53(1)(c)

As a re-enactment of a provision of the Statute of Frauds, the purpose of s.53(1)(c) must, like that of s.53(1)(b), be the prevention of fraud. But exactly what fraud is the provision trying to prevent? That question is discussed in Vandervell v IRC, the leading case on the topic. There, a beneficiary under a bare trust of shares gave an oral direction to his trustees to convey the shares to a third party, which transfer was then made. The beneficiary’s intention was that the third party would hold the shares outright. However, the Inland Revenue argued that the third party was a resulting trustee of the rights, the beneficiary’s interest still being vested in him because of his failure to comply with s.53(1)(c). The argument was rejected by the House of Lords. Section 53(1)(c) was a provision designed to protect trustees, and in the situation where the rights were no longer to be held on trust, there were no trustees to protect. The sub-section had no work to do and did not therefore apply.

Thus, it is the trustees whom the provision is designed to protect, but from what do they need protection? The answer is false allegations by someone claiming to be an assignee of the beneficiary’s interest. The difficulty for the trustee in such a case is that if they pay out to the false assignee they thereby commit a breach of trust (a wrong of strict liability) and consequently incur a liability to the true beneficiary to reinstate the trust fund. A requirement that assignments be made in writing protects the trustees because they can now, by demanding sight of the documentary transfer, ensure they pay out only to genuine assignees.

In light of this, the question arises whether Grey needs to be revisited. It will be recalled that the trustees were there directed by the beneficiary, albeit orally, to hold the rights for a new set of beneficiaries. And because they received their instructions from the beneficiary himself, they knew it was genuine. Forcing the beneficiary to put his direction in writing would tell them nothing they did not already know. It is of course different with an assignment, where the claim for payment now comes from a third party, the putative assignee, and where the trustees are consequently vulnerable to fraud. But that concern is not present in a case like Grey. Were, therefore, the courts to adopt the purposive approach of Vandervell, it might also be said that in Grey, the subsection had no work to do.

ESSENTIAL READING

- Re-read Penner, Chapter 6: ‘Formalities and secret trusts’, paras 6.13–6.42
  (‘Disposition of subsisting equitable interests: Law of Property Act 1925, s 53(1)(c)’).

At least one of the following:

- Martin, Chapter 3: ‘Requirements of a trust’, Section 2 ‘Formalities’.
- Oakley, Chapter 4: ‘The formal requirements for the creation of a trust’, Section II ‘The statutory requirement of writing’.
- Pettit, Chapter 5: ‘Formal requirements of express trusts’, Section 1 ‘Inter vivos transaction’, Part (C) ‘Dispositions of equitable interests inter vivos’.


FURTHER READING

ACTIVITY 7.2
Read and note the decision in Vandervell v IRC (1966), though ignoring for now all discussion of the option to purchase and resulting trusts. We will return to them in Chapter 12.

a. What, according to the arguments of the Inland Revenue, is the role of s.53(1)(c) in this case?

b. How successful is the Revenue’s argument in the eyes of Lords Upjohn and Wilberforce?

c. According to Lord Upjohn, what purpose does s.53(1)(c) serve?

No feedback provided.

SAMPLE EXAMINATION QUESTIONS

Question 1 How, if at all, should ss.53(1)(b) and 53(1)(c) of the Law of Property Act 1925 be reformed?

Question 2 Alfred holds 10,000 shares on trust for Peter for life, remainder to Maud. Consider the effect of the following:

a. Peter orally declares himself trustee of his interest for Carol.

b. Maud and Roger agree that Roger will exchange his unique stamp collection for Maud’s remainder interest, and Roger delivers Maud his collection in furtherance of this agreement.

c. Alfred, on the oral instructions of Peter and Maud, transfers the shares to Brian, Peter and Maud having previously instructed Brian by telephone to hold them on trust for David.

ADVICE ON ANSWERING THE QUESTIONS

Question 1 Any question which asks about the reform of statutory provisions has to first ask what problem the statute was designed to solve and how successful the solutions were in tackling it. A specific issue here concerns the age of the statutory provisions, which date back to 1677. The question which must be asked is whether the problem is one peculiar to that time.

If we start with s.53(1)(b), the first thing which needs to be done is to explain what the statute prescribes. Candidates should state that it is a provision designed to prevent fraud by excluding certain types of evidence being admitted to substantiate an allegation that a declaration of trust was made and comment on how successful it was in meeting the problems of the time. They should also explain how the provision has caused courts problems, as witness the circular logic adopted by the Court of Appeal in Rochefoucauld v Boustead, and the total mess in which we currently find the matrimonial homes cases. They might also question whether the provision is needed today, the law of evidence having improved greatly over the last 300 and more years. Support for this proposition could be sought from the observation that there is no clamour to expand s.53(1)(b) to encompass allegations that declarations of trust were made in respect of rights other than property rights in respect of land. This could be
said to show that the problems of perjury are not as great nowadays as they were in 1677. This would indicate that the best reform of s.53(1)(b) would be its abolition.

As for s.53(1)(c), candidates should once again start with its legislative history, explaining, by reference to *Vandervell v IRC*, the purpose of the provision. But since it was less about courts and more about trustees being deceived, the same call for abolition as made for s.53(1)(b) might not be appropriate. Indeed, if anything, the section might be strengthened, in two ways. First, the ambiguity as to whether it applies outside the case of trusts of land should be resolved, it being made clear that it applies to all trusts. Second, it might be worth considering whether to tighten it up by making it a condition of the effectiveness of the disposition that it be notified to the trustee. A good analogy in this respect would be s.136 of the LPA 1925, a provision concerned with the assignment of choses in action, where similar issues arise.

**Question 2** The issue in every part of this question is the same: is the transaction in question a ‘disposition of an equitable interest or trust’ and thereby void because not in writing? Since the question involves shares, there is an initial issue whether s.53(1)(c) applies to trusts other than trusts of land. That dealt with, each sub-part of the question should be taken in turn:

a. Although *prima facie* not caught by the rule, there is a danger that this could be seen as a disposition rather than a declaration because of the operation of the rule in *Grainge v Wilberforce*. Candidates should argue the merits of this dictum, and, if correct, suggest ways in which such a conclusion might be avoided.

b. This part raises questions about the effect of a specifically enforceable contract and whether the sub-trust thereby arising will also amount to a purported disposition and be invalidated by s.53(1)(c). This issue was the subject of discussion in *Oughtred v IRC* and *Neville v Wilson*. One point which needs to be asked is whether the contract here is specifically enforceable, for if it is not, no question of a constructive trust arises. That will depend on whether the shares are in respect of a private or a public company.

c. This part is a cross between the facts of *Grey* and *Vandervell*. Though there is a direction to transfer the rights held by the trustees, as in *Vandervell*, there is no intent to vest them outright in the transferee. It might, therefore, be argued that *Grey* applies and that there is a consequent need to comply with s.53(1)(c). However, as noted in the text above, there is an argument that *Grey* should be reconsidered, and this would appear to be an ideal case in which to do so.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

| I can identify the difference between substantive requirements of a declaration of trust and procedural rules relating to its proof. |
|---|---|---|
| Ready to move on | Need to revise first | Need to study again |
| ☐ | ☐ | ☑ |

| I can identify the substantive rules relating to how dispositions of interests under trusts are made. |
|---|---|---|
| Ready to move on | Need to revise first | Need to study again |
| ☐ | ☐ | ☑ |

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>7.1 Proving a declaration of trust</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>7.2 Transfer of equitable interest</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>
8  Secret trusts

Contents

Introduction ......................................................... 82
8.1  Will formalities .................................................... 83
8.2  Justifications for the admission of evidence of secret trusts ............ 85
8.3  Some specific issues ............................................. 87
8.4  What type of trust is ultimately enforced ............................ 89
Reflect and review ................................................... 92
Introduction

This chapter is concerned with secret trusts. We will first examine the rules laid down for wills by the Wills Act 1837, and why secret trusts are problematic. We will then examine two of the justifications which have been put forward to explain why evidence is routinely admitted in the case of secret trusts apparently contrary to the provisions of the statute. An important question is whether either of these justifications is sound. We will then see how the limits of the various justifications mean that courts will refuse to admit non-conforming evidence in certain cases. Finally, we will ask what type of trust is enforced where the evidence is admitted.

This chapter builds on work done in the last chapter, and you should therefore re-read that material before embarking on this topic.

Essential reading

Penner, Chapter 6: ‘Formalities and secret trusts’, paras 6.43–6.79.

Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- state the formal requirements for a valid will
- describe the problems raised by secret trusts
- analyse the different responses of the courts to secret trusts
- state when evidence of a declaration of trust which does not take the form of signed, witnessed writing will be admitted in the case of a secret trust.
8.1 Will formalities

8.1.1 The formality rules

Originally, a will could be made orally and was proved in court by the testimony of witnesses present at the time. This opened the door to fraudulent claims, and in 1677 the Statute of Frauds drastically restricted the circumstances in which oral evidence could be admitted to prove the will, and further provided that only written evidence was admissible to prove events which had happened more than six months before. The statute also provided that wills of land had to be in writing which was signed and witnessed. The Wills Act 1837 introduced a common form for both real and personal property, providing in s.9 as follows:

No will shall be valid unless –

(a) it is in writing, and signed by the testator, or by some other person in his presence and by his direction; and

(b) it appears that the testator intended by his signature to give effect to the will; and

(c) the signature is made or acknowledged by the testator in the presence of two or more witnesses present at the same time; and

(d) each witness either –

(i) attests and signs the will; or

(ii) acknowledges his signature,

in the presence of the testator (but not necessarily in the presence of any other witness), but no form of attestation shall be necessary.

It should be noted that s.9 concerns the manner in which wills are made. In this respect, it is similar to s.53(1)(c) of the LPA 1925 and not merely an evidential requirement like s.53(1)(b). A will must be made in writing and not merely evidenced by writing: see Lim v Thompson [2009] EWHC 3341 (Ch) at [25]. Nevertheless, as we shall see, courts have long been willing to give effect to secret trusts despite the failure to comply with the Wills Act 1837.

Two further provisions need noting. First, in order to ensure the impartiality of the witnesses, the legislation provides (in s.15 of the Wills Act 1837) that any ‘beneficial devise’ to an attesting witness or that attesting witness’s spouse shall be void. Note that a gift to an attesting witness does not make that witness incompetent to attest to the genuineness of the testator’s signature; the only effect is that the gift to the attesting witness or their spouse will be void. Second, s.20 provides that any alteration to the will (a codicil) must comply with the same formalities required of wills (i.e. in writing, signed and witnessed properly).

8.1.2 What are secret trusts?

There are two types of secret trust, fully secret and half secret. In a fully secret trust, the will makes no mention whatever of a trust. The testator has declared that a legatee under the will takes absolutely, but is in fact secretly a trustee who is to hold on trust for a third party. The same occurs in a half secret trust, save only that the will now contains a declaration of trust, but fails to disclose the objects of that trust. A typical form of words would be, ‘£10,000 to John on trust for the persons or purposes I have communicated to him’.

It is not always easy to tell whether a trust is fully or half secret. The essential question is whether the gift in the will appears to be intended for the recipient’s own benefit or to be held in trust. In Rawstron v Freud [2014] EWHC 2577 (Ch), a famous and wealthy artist, Lucien Freud, left the residue of his estate to his solicitor and daughter, who were the executrices of his estate. They admitted that they were secret trustees of the residue, but argued that it was a fully secret trust. The artist’s son argued that a proper construction of the entire will showed that the residue was to be held in trust and
therefore it was a half secret trust which might be invalid (see Section 8.3.1, below). The judge, Richard Spearman QC, held at [64] that ‘in the light of (a) the natural and ordinary meaning of the words used…, (b) the overall purpose of the Will, (c) the other provisions of the Will, (d) the material factual matrix when the Will was made and (e) common sense’, the residue was given to the executrices for their own benefit, and therefore the trust they admitted was fully secret.

Two questions arise. First, why are secret trusts problematic, and second, why do testators create them? As to the first, secret trusts are problematic because if they are going to be given effect by the courts, then evidence in a form not sanctioned by s.9 Wills Act 1837 will need to be admitted, for it is generally the case that the declaration of trust will not be evidenced by signed and properly witnessed writing. If the evidence is not admitted in the case of a fully secret trust, the legatee will take outright. In the case of a half secret trust, the trust will fail for want of objects, generating a resulting trust in favour of the testator’s estate. As to why testators create secret trusts, the two most common reasons are to avoid publicity and to be able to change their minds without the need for a codicil. The desire to avoid publicity comes from the fact that wills are public documents which anyone can inspect on payment of a nominal fee. If the testator wants, for example, to make provision for an illegitimate child, that might be something which they do not want placed in the public domain.

**ESSENTIAL READING**

At least one of the following:
- Martin, Chapter 5: ‘Testamentary gifts not complying with the Wills Act 1837, secret trusts’, except para.5-002.
- Oakley, Chapter 4: ‘The formal requirements for the creation of a trust’, Section III ‘Secret trusts’.
- Pettit, Chapter 7: ‘Secret trusts and mutual wills’, Section 1 ‘Fully secret and half-secret trusts’.
- Wills Act 1837, ss.9, 15, 25.

**FURTHER READING**


**ACTIVITY 8.1**

Make a short spoken presentation summarising the requirements for admission of evidence to prove a will.

No feedback provided.

**Summary**

Historically, a will could be made orally and was proved in court by the testimony of witnesses present at the time, but this was changed by the Statute of Frauds 1677. Section 9 of the Wills Act 1837 introduced a common form for both real and personal property and required that, to be valid, all testamentary dispositions be made in a signed and properly witnessed written document. Section 15 of the Act created measures to ensure the impartiality of the two signing witnesses, and s.20 made clear that any amendments to a will must meet the same formal requirements.

In the case of a fully secret trust, the will makes no mention of the trust, and in the case of a half-secret trust, though there is a declaration of trust on the face of the will, it is void for want of objects. Problems are raised by secret trusts because the evidence required to prove the making of the declaration of trust is not in the form sanctioned by s.9 the Wills Act 1837.
8.2 Justifications for the admission of evidence of secret trusts

8.2.1 The fraud theory

Why should the courts admit evidence of the declaration of a trust which is not in the form prescribed by the statute? Given that evidence not in such form has been adjudged unreliable by the legislature, it might be thought that the court should simply refuse to admit it and:

- in the case of a fully secret trust, allow the legatee to take absolutely, or
- in the case of a half-secret trust hold that the testamentary trust fails for want of objects and that there is consequently a resulting trust (see Chapter 12) in favour of the testator’s estate.

The earliest justification was based on the idea that the statutory provisions, which were originally contained in the Statute of Frauds 1677, were designed to prevent fraud, and a legatee who took on the basis that they were a trustee but who later relied on the statute to take absolutely, would be using the statute as an engine of fraud: compare Thynn v Thynn (1684) and Rochefoucauld v Boustead (discussed in Chapter 7). There are, however, a number of problems with the fraud theory. Apart from the fact that it fails to address the point that such evidence is inherently unreliable, it is circular (for the same reasons that the thinking in Rochefoucauld v Boustead is circular). Moreover, it struggles to explain the admission of evidence in cases of half secret trusts, for if the evidence is refused admission there, there will be a resulting trust for the testator’s estate and no possibility of personal gain by the secret trustee. Also, in most cases, the secret trustee is not trying to deny what happened, but honestly gives evidence of the communication and seeks the court’s advice concerning the validity of the secret trust and disposition of the estate.

In Blackwell v Blackwell, Lord Buckmaster and Lord Hailsham had to redefine the fraud which the courts were trying to prevent as not just a personal gain to the trustee but the defeating of the expectations of the secret beneficiaries or the disappointment of the wishes of the testator. If the secret beneficiary has indeed detrimentally relied on the expectation of receiving a gift from the estate, then it should be possible to provide some relief by way of proprietary estoppel, as in Thorner v Major [2009] UKHL 18, [2009] 1 WLR 776 (discussed in Chapter 6). However, this is seldom the case. It is true that in every case the testator has relied on the secret trustee’s promise to carry out the testator’s wishes, and having died, it is too late to make alternate arrangements. This form of detrimental reliance might explain the enforcement of the secret trust, but we should ask whether, and to what extent, it is reasonable for a testator to rely on an informal promise instead of setting out the terms of the trust in the will, which the testator has taken the trouble to execute.

8.2.2 The outside (dehors) the will theory

An alternative theory was put forward in Cullen v A-G for Ireland (1866) LR 1 HL 190 and adopted by Viscount Sumner and Lord Warrington in Blackwell v Blackwell [1925] AC 318. In Blackwell, the testator had made a will by which he left £12,000 to five people on trust ‘for the purposes indicated by me to them’. The court admitted the oral testimony of the trustees to identify the objects of the trust. In answer to the objection that in so doing the courts were ignoring the statutory provisions (in the words of the judges, ‘giving them the go-by’) Lord Warrington said that it must be remembered that:

what is enforced is not a trust imposed by the will, but one arising from the acceptance by the legatee of a trust, communicated to him by the settlor, on the faith of which acceptance the will was made or left unrevoked.... If the evidence had merely established who were the persons and what were the purposes indicated it would in my opinion have been inadmissible, as to admit it would be to allow the making of a will by parol.† It is the fact of the acceptance of the personal obligation which is the essential feature, and the rest of the evidence is merely for the purpose of ascertaining the nature of that obligation.

† Parol: this may also be spelled ‘parole’. It is a French word meaning ‘spoken word’. See your law dictionary for further explanations.
Viscount Sumner expressed himself in similar terms:

It is communication of the purpose to the legatee, coupled with acquiescence or promise on his part, that removes the matter from the provision of the Wills Act and brings it within the law of trusts.

There are several problems with what has been termed the ‘outside the will’ (or dehors* the will) theory.

First, it still fails to address the fundamental objection that the evidence the court admits is inherently unreliable.

Second, it assumes a dichotomy between the law of trusts and the law of wills in spite of considerable overlap, since many trusts are created by wills.

Third, it does not explain why the acceptance of the trust by the trustee should be important, since that is normally not a requirement in English law for the creation of a valid trust.

Fourth, this theory is founded on an unduly narrow interpretation of what is a will. It assumes that it is the formal document executed by the testator but this is not what the statute means. Prior to the Statute of Frauds 1677, wills could be made orally. By ‘will’ we normally mean the totality of the testator’s valid wishes concerning the distribution of their rights on their death. The intention that certain rights be held on trust for others can be regarded as part of that will.

Note that both the fraud theory and the outside the will theory are still in play, though some judges talk of the outside the will theory as representing the ‘modern view’ which explains the admission of the otherwise inadmissible evidence.

A third theoretical justification, that the doctrine of secret trusts is part of the law on incorporation by reference, cannot be accepted for a number of reasons, the most obvious of which is that the doctrine only applies to documents, whereas in secret trusts the courts will admit oral testimony.

**Essential Reading**

- At least one of the following:
  - Martin, Chapter 5: ‘Testamentary gifts not complying with the Wills Act 1837, secret trusts’, Section 6A ‘Lifetime trust outside the will’.
  - Oakley, Chapter 4: ‘The formal requirements for the creation of a trust’, Section III ‘Secret trusts’, Part 1 ‘The theoretical justification for the existence of the doctrine of secret trusts’.
  - Pettit, Chapter 7: ‘Secret trusts and mutual wills’, Section 1 ‘Fully secret and half-secret trusts’.
  - Cases: Thynn v Thynn (1684) 1 Vern 296; Cullen v A-G for Northern Ireland (1866) LR 1 HL 190; McCormick v Grogan (1869) LR 4 HL 82; In Bonis Smart [1902] P 238; Blackwell v Blackwell [1929] UKHL 1, [1929] AC 318.

**Reflection Point**

Why are secret trusts considered so important that judges are willing to accept evidence ‘which is not in the form prescribed by the statute’?

**Summary**

There are two main theories that attempt to justify the admission of the otherwise inadmissible evidence in the case of secret trusts.

1 The fraud theory. This is based on the concept that the statutory provisions were designed to prevent fraud, and that a legatee who had agreed to be a trustee and who was only given the rights on that basis but who later relied on the statute to take absolutely, would be using the statute as an engine of fraud. This theory creates
some problems, however. It fails to deal with the point that the courts are admitting unreliable evidence, it is circular, it struggles to explain the admission of evidence in the case of half secret trusts and it does not explain the many cases in which secret trustees honestly give evidence of the secret trust. In both Blackwell v Blackwell and Cullen v A-G for Northern Ireland an alternative theory was put forward to attempt to resolve this problem.

2 The outside (dehors) the will theory. This theory also raises a number of problems. It too fails to address the fundamental objection that the evidence the court admits is inherently unreliable, it falsely assumes a dichotomy between the law of trusts and the law of wills, it fails to explain why the acceptance of the trust by the trustee should be important and it is founded on an unduly narrow interpretation of what is a will.

Courts make reference to both theories, though some regard the dehors the will theory as the modern justification of admission.

8.3 Some specific issues

We have seen that, in general, courts will in cases of secret trusts admit evidence not in the form sanctioned by the statute to prove the declaration of trust. We have also seen that the various explanations for doing so do not stand up. For the moment, however, we must accept that, using either the fraud theory or the outside the will theory, this practice is justified. There are, however, a number of situations in which courts still refuse to admit the non-conforming evidence.

Problem questions on secret trusts generally revolve around the question whether in the case of the particular secret trusts described, the non-conforming evidence will be admitted. Some of the main factors which stand in the way of admission are set out below. You should note, however, that this list is not exhaustive.

8.3.1 Timing of acceptance

As we have seen, both the fraud theory and the outside the will theory require the secret trustee to have accepted, or at least acquiesced in, the office of trusteeship. Both acceptance and acquiescence require at the very least that the declaration of trust be communicated to the secret trustee. The crucial question is when that communication must take place.

For fully secret trusts, the rule is that the communication to the secret trustee be made before the testator’s death. The reason is that if the trustee did not know they were intended to be a trustee, they could hardly be said to have accepted or acquiesced in their appointment: Re Boyes [1884] 26 Ch D 531. However, the rule is more restrictive for half secret trusts, where, at least according to the Court of Appeal in Re Keen [1937] Ch 236, the communication must not take place after the execution of the will. The reason for this was that otherwise the testator would be free to change their will without the execution of a codicil.

The difficulty with this reasoning is that, if the trust really does arise outside the will, then a change of mind over the terms of the trust is not a change in the will at all. Moreover, it seems strange that a communication post execution is acceptable for a fully secret but not for a half-secret trust. Several other jurisdictions have refused to follow this rule and you should ask whether it can be supported. It should also be noted that the finding in Re Keen is arguably obiter as the secret trust was struck down on the separate and logically prior ground of inconsistency between the time at which the terms of the trust were communicated to the trustees and the will’s account of this event.

Further problems arise where there are intended to be two or more trustees but communication is not made to all of them. Are the trustees who have not been told bound by the trust or can they take the rights for themselves? The rules are contained in Re Stead [1900] 1 Ch 237, a fully secret trust case. They provide that where the trustees take as tenants in common, then only those who know of the trust are
bound, but where they take as joint tenants, then it has to be asked whether the communication was made before or after the execution of the will. If the former, then all will be bound, but if the latter, only those who were told. There is no case law on this point with regard to half-secret trusts, though in such a case they will almost certainly take as joint tenants and if Re Keen is correctly decided, the communication will anyway have to precede the execution of the will.

8.3.2 Predecease of the secret beneficiary

What happens if the secret beneficiary predeceases the testator? The starting point, it is suggested, is to ask what would have been the result had this trust been expressed in the form required by s.9 of the Wills Act 1837. The answer is that the doctrine of lapse would apply and the gift will fall into residue. There is no good reason why the same result should not obtain where the declaration of trust is not proved by signed, witnessed writing. However, in Re Gardner (No 2) [1923] 2 Ch 230, Romer J held that the secret trust was an inter vivos trust which was in existence before the death of the beneficiary, and therefore passed to her estate. The problem with this reasoning is that there could be no inter vivos trust because there was no self-declaration of trust and therefore the intended trust had not been constituted before the death of the testator.

8.3.3 Predecease of the secret trustee

If the trust had been spelt out on the face of the will, it is clear that it would not fail if the trustee predeceased the testator. Applying the rule that ‘equity will not allow a trust to fail for want of a trustee’, a substitute trustee would be appointed. The difficulty here, however, is that the secret trust doctrine seems to be based on an acceptance or acquiescence by a particular trustee and it is because of that agreement that the situation is taken out of the province of the statutory rules on formality. If that is right, then the doctrine of lapse should apply and the gift should fall into residue. The textbooks, however, generally distinguish between fully secret and half secret trusts in this regard, arguing for failure only in the case of the former.

8.3.4 Witnessing by secret beneficiary

As we have seen, s.15 of the Wills Act 1837 makes void any gift to an attesting witness or their spouse. If a trust in favour of a witness had been included in the will, then it is clear that the witnessing beneficiary could not take the benefit of that trust, which would then be void for want of objects and give rise to a resulting trust for the residuary legatees. It might be thought that the position should be no different in the case of a secret trust. However, in Re Young [1951] Ch 344, Dankwerts J upheld a half secret trust in favour of a witness. Since the trust took effect outside the will, the Wills Act rules did not apply.

8.3.5 Witnessing by secret trustee

There is normally no problem with a trustee witnessing the will, for the trustee can take no benefit from their office as trustee, but the question is difficult in the case of secret trusts. If the trust is fully secret, then the operation of s.15 will mean that the rights will not reach the trustee and so the trust will never be constituted. In the case of a half secret trust, admissible evidence will show the court that the legatee is a trustee and so arguably s.15 would not apply.

Self-assessment questions

1. What is the difference between a fully secret trust and a half secret trust?
2. What are the justifications for the admission of non-conforming evidence in the case of secret trusts?
3. What does it mean to say that a gift ‘falls into residue’?
4. Can a trustee witness a will, and if so, in what circumstances?
Summary

1. Timing of communication of the trust: In the case of both fully and half-secret trusts the trustee must have accepted or acquiesced in the office of trusteeship. However, the crucial question is when that communication has to be made. In fully secret trusts, it must be before the death of the testator. In half-secret trusts, it must precede the death of the testator and the execution of the will, although the reasons justifying the difference are doubtful.

2. Where the secret trust assets are given to two or more trustees but communication is not made to all of them, Re Stead provides a rule for determining which of them is bound in the case of fully secret trusts. Only the trustee to whom communication is made is bound unless the trustees take as joint tenants and communication is made before the making of the will, in which case all are bound. However, the justification of this rule is doubtful.

3. If the secret beneficiary predeceases the testator, the doctrine of lapse should apply and the gift should fall into the residue. Romer J’s decision to the contrary in Re Gardner (No 2) is doubtful.

4. If a half secret trustee dies before the testator, it is said that the trust will not fail because ‘equity will not allow a trust to fail for want of a trustee’. The case is less certain for a fully secret trust, in particular following the fraud theory, where the decease of the secret trustee would ensure that no fraud could occur. But query whether the first proposition is correct.

5. In Re Young, Dankwerts J upheld a secret trust in favour of a beneficiary who witnessed the will on the basis of the dehors the will theory.

6. If a fully secret trustee witnesses the will, the operation of s.15 will mean that the rights will not reach the trustee and so the trust will never be constituted, unless some extension of the dehors the will theory is brought into play. In the case of a half-secret trust, s.15 should not apply as the will itself shows that the legatee is intended to be a trustee, but if this is correct, then Re Young must be wrong, for the dehors the will theory cannot save a gift in both the case of a witnessing beneficiary and the case of a witnessing trustee.

8.4 What type of trust is ultimately enforced

What type of trust is a secret trust? More specifically, is it express or constructive? We saw in Chapter 7 how the trust in Rochefoucauld v Boustead was express, despite the fact that some later cases misclassified it as constructive. Perhaps the same is true of secret trusts, with the fraud and outside-the-will theories providing justifications (albeit, not very strong ones) for the admission of evidence of a declaration of trust not in a form sanctioned by statute. If so, the trust which is given effect is a trust which arises directly from an expression of intention to create a trust (i.e. it is an express trust). Alternatively, secret trusts might be regarded as constructive, with the testator’s detrimental reliance on the secret trustee’s undertaking providing a sufficient reason to impose a trust even though their informal arrangement was ineffective to create an express trust. This could explain why timely communication to and acceptance by the secret trustee are required, for they are not requirements to create a valid express trust, which can be created even though the intended trustee is wholly unaware of its existence: Smith v Wheeler (1671) 1 Lev 279, 83 ER 406; Siggers v Evans (1855) 5 E&B 367, 119 ER 518.

Does it matter whether we class secret trusts as express or constructive? It would certainly help us better understand why they arise. It might also be argued that it matters in the case of a secret trust of an interest in land where there is no written evidence of a declaration of trust. Having surmounted the hurdle of s.9 of the Wills Act 1837, would the claimant be defeated by s.53(1)(b) of the LPA 1925? Such a result would be strange, for the formality requirements of s.9 are more onerous than those of
s.53(1)(b). Nourse LJ’s comments in Sen v Headley [1991] EWCA Civ 13, [1991] Ch 425 regarding a donatio mortis causa of land should apply with equal force to a secret trust:

A donatio mortis causa of land is neither more nor less anomalous than any other. Every such gift is a circumvention of the Wills Act 1837. Why should the additional statutory formalities for the creation and transmission of interests in land be regarded as some larger obstacle?

The trust in Sen v Headley was clearly and properly identified as constructive and so exempted from the operation of s.53(1)(b) by s.53(2). If secret trusts are also constructive, then they too are exempt, but even if they are express, the reasons for ignoring the Wills Act 1837 should also apply to s.53(1)(b).

**Essential reading**

At least one of the following:

- Martin, Chapter 5: ‘Testamentary gifts not complying with the Wills Act 1837, secret trusts’, Section 6B ‘Express or constructive trust’.
- Oakley, Chapter 4: ‘The formal requirements for the creation of a trust’, Section III ‘Secret trusts’.
- Pettit, Chapter 7: ‘Secret trusts and mutual wills’, Section 1 ‘Fully secret and half-secret trusts’.
- Cases: Re Fleetwood (1880) 15 ChD 594; Re Boyes (1884) 26 Ch D 531; Re Bailie (1886) 2 TLR 660; Re Gardner (No 2) [1923] 2 Ch 230; Re Keen [1937] Ch 236; Re Colin Cooper [1939] Ch 811; Re Browne [1944] IR 90; Re Edwards [1948] Ch 440; Re Young [1951] Ch 344; Re Bateman’s WT [1970] 3 All ER 817; Ottaway v Norman [1972] Ch 698; Re Snowden [1979] Ch 528; Ledgerwood v Perpetual Trustee (1997) 41 NSWLR 532.

**Activities 8.2–8.5**

8.2 Compare the formality rules of s.53(1)(b) of the Law of Property Act 1925 and s.9 of the Wills Act 1837. Which is the more stringent? And why? In particular, why was s.15 of the Wills Act 1837 enacted?

8.3 In what way are secret trusts in conflict with these formality rules?

8.4 Read carefully the speeches in Blackwell v Blackwell. How do the different judges formulate their justifications for not insisting on the strict formality requirements of the Wills Act? Are they convincing?

8.5 Go through the specific factors which might disqualify non-conforming evidence in the case of a secret trust from being admitted, asking yourself whether it makes any difference to the result which justification, fraud or dehors, is used.

**Further reading**

- Perrins, B. ‘Can you keep half a secret?’ (1972) 88 LQR 225.
SAMPLE EXAMINATION QUESTIONS

Question 1  Is there yet any coherent justification for the admission of non-conforming evidence in the case of secret trusts?

Question 2  Peter has recently died. By his will, he left his vast shareholding to his close friend, Denis. Prior to his death, he told Denis to hold the shares on trust for Mary, Peter’s illegitimate daughter. He also left his house to Robert, ‘who has already been informed in writing that it is to be held in trust’. In fact, Robert had been told by Peter before the will was made that the house was to be held for Mary, though orally and not in writing. The two witnesses to the will are Denis’s wife, Jane, and Mary.

Advise Laura, Peter’s residuary legatee.

ADVICE ON ANSWERING THE QUESTIONS

Question 1  A good answer to this question would start by outlining what a secret trust is and why people create them. It would then go on to explain why secret trusts are problematic and how the courts have managed to admit the non-conforming evidence, first through the fraud theory and later through the dehors the will theory. Having outlined the various justifications for admission, a critique of those justifications should be given. Some indications of what might be said are outlined above and need not be repeated here.

Question 2  In any problem question, you should start by outlining the issues raised. The first is obviously the general question of whether evidence not in the form required by the statute will be admitted to prove the declaration of trust. The more specific points raised by the question are the inconsistency over the method of communication, the fact that the subject-matter of the trust is an interest in land and there does not seem to be any written evidence of that declaration to satisfy s.53(1)(b), the fact that the secret beneficiary is a witness to the will, and finally, that the secret trustee’s spouse is the other witness.

As to the general question of the admission of evidence to prove the declaration of trust, a brief outline of the fraud theory and the outside the will theory need to be given. As this is a problem question rather than an essay, it is not so vital that a critique of these two theories be provided. Once these two theories have been outlined, the question then is how they apply to the specific problems raised.

The first is the inconsistency between the terms of the will (‘notified in writing’) and the evidence sought to be admitted (‘communicated orally’). This point forms the narrow ratio of Re Keen. Candidates should outline the rule laid down by Re Keen and then apply it to the facts of this case. They might then raise the question whether an inconsistency such as that in Re Keen should be fatal, for in a fully secret trust the fundamental inconsistency between what the will says (that the legatee takes absolutely) and the evidence admitted (that the legatee takes as trustee) seems never to have been an issue.

The second issue concerns the fact that the subject-matter of the trust is a title to land but the declaration of trust cannot be proved by written evidence as required by s.53(1)(b) LPA 1925. There are two issues here, both of which are discussed above. First, is a secret trust an express or a constructive trust? Second, if it is an express trust, will such a finding be necessarily fatal?

The third issue is the witnessing of the will by the secret beneficiary. Candidates should explain the usual consequences of beneficiaries of trusts witnessing wills (the avoidance of their gift) and note the different conclusion reached in the case of secret trusts by Dankwerts J in Re Young.

The fourth and final issue is the witnessing of the will by the spouse of the secret trustee. Candidates should explain what would normally happen in such a case (i.e. if the trust was not secret). Candidates should then explain that though the act of witnessing might have been problematic had the trust been fully secret, in the case of a half-secret trust this should not cause problems.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th></th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can state the formal requirements for a valid will.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can describe the problems raised by secret trusts.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can analyse the different responses of the courts to secret trusts.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can state when evidence of a declaration of trust which does not take the form of signed, witnessed writing will be admitted in the case of a secret trust.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked 'need to revise first', which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th></th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>8.1 Will formalities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8.2 Justifications for the admission of evidence not in the form sanctioned by the statute</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8.3 Some specific issues</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8.4 What type of trust is ultimately enforced</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
9 Promises to create trusts

Contents

Introduction ......................................................... 94

9.1 Promises in deeds ............................................ 95

9.2 Promises for consideration ................................. 98

9.3 Promises and detrimental reliance ...................... 99

Reflect and review .................................................. 102
Introduction

This chapter is concerned with promises to create trusts which have not been performed. The starting point is to appreciate that a bare promise is unenforceable in English law. This is the view of both the common law and equity. There are only three types of promise which courts will enforce:

- promises in deeds
- promises given for consideration
- promises detrimentally relied upon.

It is not, however, enough to decide that a particular promise is enforceable. We must also ask who it is who wishes to enforce it, and in which court.

This chapter builds on work done in Chapter 6, and you should re-read that chapter before embarking on this topic. It also requires knowledge of the contractual rules of privity and of consideration, and you should go back over the work you did on those topics in the law of contract.

Essential Reading

- Re-read Chapter 6: ‘Creating express trusts II: constitution’.
- Penner, Chapter 8: ‘The constitution of trusts’, paras 8.25–8.64.

Learning Outcomes

By the end of this chapter and the relevant reading, you should be able to:

- state the circumstances in which promises to create trusts will be enforced
- identify the persons who can enforce such promises
- describe how promises to create trusts are enforced
- critically appraise those decisions which deny the enforcement of promises.
9.1 Promises in deeds

9.1.1 The basic rule

A promise contained in a deed is called a covenant. Where a promise is contained in a deed it can be enforced at common law by those who are party to it. Thus, if I execute a deed by which I promise you that I will give you £10 for your birthday, you can sue me at law for damages to compensate you for your loss of expectation if I do not make good my promise. It does not matter that you gave no consideration in return, or, in other words, that we are dealing with a ‘voluntary covenant’. Thus, in *Cannon v Hartley* [1949] Ch 213, a father promised his daughter by deed that he would pay her any sum exceeding £1,000 which he received under his own father’s will. When he failed to do so, she successfully sued him at law for the amount she would have obtained had he kept his promise. However, we should note that equity will enforce some promises if made for consideration, but will not enforce a promise merely because it is made by deed. In such a case, equity leaves the promisee to their remedy at common law.

Even at common law, it is not enough to show that the promise is contained in a deed. There is the further issue of privity. Is the person seeking to enforce the promise a party to the deed? Suppose, for example, that I make a promise by deed to your brother that I will make a gift to you of £10. Only those to whom the promise was made can enforce it, and you are not such a person. Note that this rule was not changed by the enactment of s.56 of the LPA 1925. Whether it was changed by the Contracts (Rights of Third Parties) Act 1999 depends on whether a voluntary promise in a deed is a contract. The view taken by the authors of this guide is that it is not.

The typical scenario

The typical case involving trusts is where A promised B by deed that they would transfer rights to B for B to hold on trust for C. There are two separate issues. First, is the promise enforceable, and second, by whom? We need to consider these questions from the point of view of enforcement by both B and by C. For reasons which will become apparent later, it is best to begin with C.

9.1.2 Enforcement by the intended beneficiary

The immediate problem for C is that they are not party to the deed. In other words, the promise was made to B, not C. However, there are three situations in which C will be able to enforce the promise.

a. C is made party by statute

If the Contract (Rights of Third Parties) Act 1999 applies to voluntary covenants (which is doubtful), then assuming the requirements of the Act are satisfied, C would be able to enforce the covenant at law and obtain damages. However, the covenant would still not be enforceable in equity (via an order for specific performance). This might make a difference in the event of A’s insolvency (see below).

b. C is within the marriage consideration

The word ‘consideration’ nowadays has a technical meaning in the law of contract of *quid pro quo*. It originally meant the reason for doing something. The consideration for a promise was the reason for a promise. This old meaning still lingers on in the case of marriage settlements (described in Penner, Chapter 8, paras 8.28–8.29 (‘Covenants to settle and marriage settlements’)). At one time, it was traditional upon marriage for the bride’s father to set up a trust for the husband and wife for their joint lives and the survivor for life, with the remainder for any children of the marriage and, if there are no children, for the wife’s next of kin. The wife would also enter into a covenant whereby she promised to convey to the trustees any rights she might later receive above a certain value to be held on the same trusts. The parties to this deed would be the wife, her husband and the trustees. As the ‘consideration’ for her doing so was to provide for her family, any children or grandchildren were seen by courts of equity (though not the common law) as ‘within the marriage consideration’. Accordingly,
they were able to enforce the covenant if broken, albeit only through a claim for specific performance and not damages (a common law response). Moreover, an application of the magic formula that 'equity looks upon that as done which ought to be done' meant that the wife was now a constructive trustee of any rights she received. This would certainly have advantages if the wife became bankrupt (and also had implications for the running of limitation periods (i.e. the times when legal actions in respect of the rights in question might lapse)). However, the wife’s next of kin were not within the ‘marriage consideration’, and, not being parties to the covenant, they had no claim at law or in equity.

c. Trust of the right to sue on the covenant

B is of course the one person who does not suffer from problems of privity. Being a party to the covenant, B will have a right to sue A at common law for non-performance. An argument has sometimes been made that B holds that common law right to sue on trust for C. If this argument (the ‘trust of the covenant’ argument) is made out, then C can compel B to exercise the right and sue A. The assumption is that B would recover substantial damages at common law from A which B would then hold on trust for C.

There are two difficulties standing in the way of this argument, both of which are illustrated by Re Cook’s ST[1965] Ch 902. The first is that it will almost always be the case that the requisite declaration of trust of the right to sue will not be present on the facts (i.e. there will be no particular further intention than the one expressed in the deed). There are a number of academic authorities who argue that such an intention should be found from the mere fact that the promise to create a trust was contained in a deed, but it is difficult to see why the court should impose a trust, for that is what it would be, in these circumstances. You should therefore ask yourself whether these views can be justified. The second, and arguably unjustified, objection is that the trust of the covenant argument has been said only to work in the case of rights which the covenantor had at the time they made the covenant and not in respect of rights to be acquired later (after-acquired property).

9.1.3 Enforcement by the intended trustee

Assume that none of the situations outlined above apply, with the result that C cannot enforce the promise to create a trust in his favour. We have already seen how B does not suffer from the cause of C’s inability to enforce, a lack of privity, for the covenant was made with B. Therefore B undoubtedly has a claim at law for breach of covenant but will not be able to enforce it in equity. The enforcement of this claim, however, is far from straightforward, for there are a number of decisions which say that B will be prevented by a court of equity from suing A at law.

The authorities

In Re Pryce [1971] Ch 234 the trustees of a marriage settlement (B) sought the direction of the court whether they were bound to sue the wife (A) for non-performance of her covenant. There were no children of the marriage, so the only person who could possibly benefit was the wife’s next of kin (C). Eve J directed the trustees that they ought not to sue, because to do so would give C by indirect means what C could not obtain directly. In saying this, Eve J arguably went beyond the rule we encountered in Chapter 6, that ‘equity will not assist a volunteer to perfect an imperfect gift or trust’. The trustees were not asking for equity’s assistance, but merely a ruling on whether they were required to sue. However, the case was followed by Simonds J in Re Kay [1939] 1 Ch 329 and Buckley J in Re Cook’s ST. These cases have never been overruled, though it should be noted that they are only decisions at first instance.

Substantial or nominal damages?

Even if a court were to accept that these authorities were wrongly decided, there is the further question of what damages B would recover by suing A at law. Are they substantial or only nominal? The normal measure of damages will be measured by the
equity and trusts  9  promises to create trusts

loss of the expectation (i.e. substantial damages). There is an argument which says that
B suffers no loss of expectation, because had the covenant been performed, B would
be a trustee and a trustee makes no personal gain from their trusteeship. B is therefore
no worse off because of the non-performance. The person who has lost out is C, and B
cannot recover for C's losses. All that B is entitled to is an order for nominal damages
and for this reason (though not those given in the case) Eve J was correct in Re Pryce to
deny to B the ability to sue A at law.

The problem with this argument, however, is that it forgets that B's claim is being
brought at law, and at law B would hold any rights transferred to him in performance
of the covenant for himself, and not for C, for the common law does not recognise
trusts. Thus, in the common law's eyes – and those are the only eyes that matter for
the moment – B has suffered a substantial loss and so should recover substantial
damages. While this seems correct, and we assume that B should be able to sue for
substantial damages at law, this result leads to a further difficulty.

Even if B were to recover substantial damages, would B necessarily hold them on
trust for C? There is an argument which says that B would in fact hold the damages on
resulting trust for A, and would therefore be immediately liable to repay it to A, the
person B had just sued to recover it. This circularity of action is in nobody's interest,
and so the decision of Eve J in Re Pryce is ultimately correct (though again not for the
reasons there stated). But how can it be said that there is a resulting trust for A?

The argument proceeds as follows:

1. Going back to our discussion of the question whether C could enforce the covenant
   in C's own right, we said that one situation in which C could was where there was
   found to be a trust of the benefit of the covenant in C's favour.

2. But to get to the point at which we are now, we have assumed that this option is
   not available on our particular facts.

3. It is then argued that, the trust of the benefit of the covenant in favour of C having
   failed, there must be a resulting trust of the benefit of the covenant in favour of A.

We will encounter resulting trusts again in Chapter 12 and you would do well to return
to this part of the syllabus when you know what resulting trusts are and when they
arise. For the moment, we need know only that they are trusts under which the right
is held on trust for the transferor of the right, and that one instance in which they
arise is where rights are transferred on trusts which fail, for example, for uncertainty
of objects. The trust of the covenant here having failed, it is argued there is then a
resulting trust of the right to sue on the covenant in favour of the transferor, A. Since
the right to sue is held on trust for A, so will be any damages acquired through the
exercise of that right.

The difficulty with this argument is that any trust in favour of C cannot be said to have
'failed' at all. It was simply the case that no trust in favour of C arose because there was
no declaration of trust in C's favour. In other words, it was not the trust which failed,
but only the argument that there was a trust. As we saw in our discussion of Re Adams
& Kensington Vestry in Chapter 5, it is wrong to talk of a trust failing in circumstances
where there is simply no declaration of trust at all. A transfer which is not a transfer
on trust is an outright transfer, not a failed trust. If we do not find a trust in favour of
C, therefore, B will hold the right to sue absolutely, not on resulting trust for A. Any
damages B receives when suing under the covenant would not be held on trust for A
either. The damages will instead be held by B on trust for C, for the damages are simply
the law's substitute for performance of the covenant.

essential reading

At least one of the following:

- Martin, Chapter 4: 'Constitution of trusts. Equity will not assist a volunteer',
  Sections 4 'Covenants to settle', 5 'Action for damages by the trustees. Trusts of
  choses in action', 6 'Trusts of future property'.


- Oakley, Chapter 5: ‘The constitution of a trust’, Section IV ‘When a trust is incompletely constituted, when will the intended beneficiaries have a contractual remedy?’.
- Pettit, Chapter 6: ‘Completely and incompletely constituted trusts’.
- Cases: Davenport v Bishopp (1843) 2 Y & CCC 451; Fletcher v Fletcher (1844) 4 Hare 67; Lloyds v Harper (1880) 16 Ch D 290; Re Plumptre’s Marriage Settlement [1901] 1 Ch 609; Re Ellenborough [1903] 1 Ch 697; Pullan v Koe [1913] 1 Ch 9; Re Cavendish-Browne’s Settlement Trust [1916] WN 341; Re Pryce [1917] 1 Ch 234; Re Kay [1939] 1 Ch 329; Re Schebsman [1944] Ch 83; Cannon v Hartley [1949] Ch 213; Re Cook’s Settlement Trusts [1965] Ch 902.

FURTHER READING

ACTIVITY 9.1
Make a short spoken presentation explaining why some commentators consider that the cases of Re Pryce, Re Kay and Re Cook’s ST are wrongly decided.

SELF-ASSESSMENT QUESTIONS
1. What is a covenant?
2. What is a deed?
3. What is ‘marriage consideration’?
4. What is the trust of the covenant argument? What are the views for and against it operating to allow C to sue on a covenant?
5. What are the arguments for and against saying that Eve J’s decision in Re Pryce, that a trustee will be directed not to sue on a gratuitous covenant to settle, was correct? (Remember to consider how the question, for whom does a trustee who successfully sues and gets substantial damages hold them, bears on the issue).

Summary
A covenant is a promise contained in a deed. Unless made for consideration, it can be enforced only at common law and only by those party to it.

Where A gratuitously covenants to transfer rights to B on trust for C, C can enforce the covenant where C is privy to the covenant, or is made privy under the Contract (Rights of Third Parties) Act 1999 (though it is doubtful whether the statute applies to covenants), or where C is within the ‘marriage consideration’ in the case of marriage settlements. Where B holds the right to sue on trust for C, then C can direct B to sue A. However, a trust in such circumstances is unlikely to be found. First, the requisite intention, whatever that might be, is generally missing and difficult to conceive in any case; second, there is authority that this concept cannot apply to after-acquired property.

B, of course, is a party to the covenant and so can enforce it at common law. However, B may be barred from doing so by the Re Pryce line of cases, and even if successful in their action for substantial damages, it is not clear whether equity will require B to hold them on trust for C rather than on resulting trust for A.

9.2 Promises for consideration
If consideration in the normal contractual sense has been given in exchange for the promise to set up a trust (or to make a gift), and that promise has not been performed, the promise will be enforceable at law through a claim for damages or, if damages are thought to be an inadequate response, by an award of specific performance in equity.
There still, of course, remains the problem of privity, for the promisee might not be the intended beneficiary/donee. Thus, in *Re Cook’s ST*, the court held that it did not help someone in the position of C to show that consideration for A’s promise had been given by B. As Buckley J explained, ‘conduct by A which is unconscientious in relation to B so as to entitle B to equitable relief may not be unconscientious in relation to C so that C will have no standing to claim relief notwithstanding that the conduct in question may affect C’. *Re Cook’s ST* was of course decided before the enactment of the Contract (Rights of Third Parties) Act 1999, and it should now be asked whether s.1 of that Act might give the beneficiary/donee a right to sue in their own name.

**ESSENTIAL READING**

At least one of the following:

- Oakley, Chapter 5: ‘The constitution of a trust’, Sections IV(1) ‘A simple contract to create the trust’ and IV(2) ‘A specialty contract or covenant to create the trust’.
- Case: *Re Cook’s ST* [1965] Ch 902.

**FURTHER READING**


**9.3 Promises and detrimental reliance**

Although there are no cases on this topic, there are some concerning promises of outright gifts, and it is assumed that a promise to create a trust will be treated no differently from them. Normally, the promisee would have no redress if such a promise is not to be performed. Things will be different, however, where the promisee has relied on the promise to their detriment (i.e. changed their position to their detriment in the reasonable belief that the promise would be performed). In such a case, equity (though not the common law) will compel the promisor to perform their promise. In the interim, the promisor will arguably hold the right in question on constructive trust for the promisee.

**ESSENTIAL READING**

At least one of the following:

- Martin, Chapter 12: ‘Constructive trusts’.
- Oakley, Chapter 10: ‘Constructive trusts’, Sections IV(4)–V(3).
- Pettit, Chapter 10: ‘Common intention constructive trusts; proprietary estoppel; licences’, Section 2 ‘Proprietary estoppel’.

**FURTHER READING**

- Barton, J.L. ‘Trusts and covenants’ (1975) 91 LQR 236.
- Hornby, J. ‘Covenants in favour of volunteers’ (1962) 78 LQR 228.

**ACTIVITIES 9.2 AND 9.3**

9.2 Read *Pullan v Koe* [1913] 1 Ch 9 and *Re Plumptree’s ST*. Exactly when and by whom can a marriage settlement be enforced? How is it enforced?
9.3 Read *Re Basham, Eves v Eves* [1975] 3 All ER 768 and *Dillwynn v Llewellyn*. What role does detrimental reliance play in each of these cases?

**SAMPLE EXAMINATION QUESTIONS**

**Question 1** The rule is ‘Equity will not assist a volunteer to perfect an imperfect gift’, not ‘Equity will stand in the way of a volunteer suing for non-performance of a promise to give’.

Discuss.

**Question 2** Toby covenants that he will convey £10,000 from the £100,000 currently in his account with the London Bank plc and any winnings he might receive from next week’s lottery draw to Ella to hold on trust for James. Although he subsequently wins £1 million on the lottery, Toby fails to do either of these things.

Advise James. Would it help him if he could persuade Ella to sue Toby?

**ADVICE ON ANSWERING THE QUESTIONS**

**Question 1** This question is directed to the attitude of the courts to the enforcement of promises to create trusts. Specifically, it is directed to the judgment of Eve J in *Re Pryce*.

A good answer would begin with a discussion of equity’s attitude to imperfect trusts/gifts, pointing out the general rule in *Milroy v Lord* and the various exceptions to it. It would not, however, be appropriate in this question to examine those exceptions in detail, merely to note their existence.

Having outlined Equity’s negative approach to imperfect trusts/gifts, the situation where Equity could be said to stand in the way of the enforcement of a promise to give should be described. The case in which this happened was of course *Re Pryce*, and the facts of that case should be recounted, along with a general discussion of the enforcement of promises to settle. The main question is whether the decision in *Re Pryce* was correct, either on its own reasoning or for reasons which are not contained in the judgment. At this point, the wealth of academic literature on this topic should be discussed.

**Question 2** We need to consider the position of both Ella and James with regard to the enforcement of this promise. It is best to start with James, the putative beneficiary, and only then go on to consider the position of Ella, the putative trustee.

James will only be able to enforce this covenant in three circumstances:

a. he is privy to the covenant;

b. it is a marriage settlement and he is within the marriage consideration;

c. the right to sue on the covenant is held for him on trust.

We will consider each in turn.

**Privity**

Since the covenant is made with Ella and not James, James is not a party to the covenant made by Toby. It might be the case, however, that he is given the rights of a party by the Contracts (Rights of Third Parties) Act 1999, which abolished one limb of the privity rule in contract, viz. that a third party could not take a benefit under a contract. Whether this Act confers on James the right to sue depends on two things:

a. whether the Act applies to voluntary promises in deeds, and

b. if it does, whether this covenant is caught by s.1 of the Act.

Whether the Act applies depends on how the word ‘contract’ in the 1999 Act is interpreted. Understandably, the Act gives no definition of what is meant by this word. Generally, however, a contract is a bargain, an exchange of promises for consideration. This is not what we have here. We have only a unilateral promise for no consideration. On that basis, it is arguable that such a promise, though enforceable at common law,
is not a contract. There is no authority on this question. If, contrary to this argument, voluntary covenants were to be considered as species of contracts, then it has to be asked whether the specific provisions of the 1999 Act apply. Given that the deed does not expressly give James the right to sue, the question will be whether, under s.1(1) (b), the term purports to confer a benefit on him. It clearly does and there seems to be nothing in the deed to show that James was not intended to be able to enforce the promise: s.1(2). There is then the further question what response James will get. The answer is that he will be able to enforce the promise in the same way as if he was named as a party: s.1(5). And though he will be able to claim common law damages for loss of expectation, he will not be entitled to specific performance, as equity always refuses to grant specific performance of a voluntary covenant.

**Marriage settlement**

If this is a marriage settlement (we are not told either way) and James is within the marriage consideration (again we are not told), then James can enforce the promise in equity. In the meantime, applying the maxim ‘Equity regards as done that which ought to be done’, Toby will hold the rights on constructive trust for James.

**Right to sue on the covenant held on trust**

There is no doubt that a chose in action can form the subject-matter of a trust. There is no doubt also that Ella has the benefit of a chose in action, the right to sue Toby under the covenant. The question is whether we can say that Ella holds her right on trust for James. The problem is that there was no declaration of trust by Toby to this effect. Note the academic arguments which say that a trust, presumably some sort of constructive trust, should always be found in such cases. Note the further difficulty that Buckley J said in *Re Cook* that a trust of the right to sue is only possible in the case where the covenant relates to present rather than future rights, and that the money won on the lottery was not a present right at the time the covenant was made. You should discuss whether Buckley J was right in his view.

On the assumption that none of these exceptional cases avail James, he will not be able to enforce the covenant. Then comes the question whether Ella will be allowed to do so. She, of course, is party to the deed, so would seem to have an unquestionable right to sue at common law. The problem is that three cases from equity, *Re Pryce*, *Re Kay*, and *Re Cook*, stand in her way. You should discuss the reasoning in *Re Pryce*, with the aim of showing that it cannot stand. Further discussion should then be made concerning the question whether the decision can be defended on other grounds, those being (i) that any damages Ella could recover from Toby at law would be nominal, and (ii) even if they were substantial, they would be held on resulting trust for Toby. Arguments as to why both those propositions are false have been rehearsed above.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

- **I can state the circumstances in which promises to create trusts will be enforced.**
  - [ ] Ready to move on
  - [ ] Need to revise first
  - [ ] Need to study again

- **I can identify the persons who can enforce such promises.**
  - [ ] Ready to move on
  - [ ] Need to revise first
  - [ ] Need to study again

- **I can describe how promises to create trusts are enforced.**
  - [ ] Ready to move on
  - [ ] Need to revise first
  - [ ] Need to study again

- **I can critically appraise those decisions which deny the enforcement of promises.**
  - [ ] Ready to move on
  - [ ] Need to revise first
  - [ ] Need to study again

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>9.1 Promises in deeds</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9.2 Promises for consideration</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9.3 Promises and detrimental reliance</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
10 Purpose trusts I: public purposes

Contents

Introduction ................................................................. 104

10.1 Charitable status ......................................................... 105

10.2 The meaning of ‘charity’ ............................................... 106

10.3 The public benefit requirement ..................................... 111

10.4 Contaminating non-charitable elements .......................... 113

10.5 Failure of charitable trusts: the cy-près doctrine ................. 113

Reflect and review ......................................................... 118
Introduction

The question addressed in both this chapter and the next is whether it is possible to have a trust, not persons, but for a purpose. Where the purpose is public, that is, a purpose recognised by the law to be charitable, then it is indeed possible to have such a trust. The difficult question is in deciding what amounts to a charitable trust. In this chapter, we will consider the various types of charitable purposes, the over-arching requirement of public benefit which is considered essential to charitable status, and elements of a purpose which may contaminate it, rendering it not exclusively charitable. We will then consider a special doctrine, cy-près, which applies on the failure of a charitable purpose. The Charities Act 2006 was a major development in the law relating to charity. It has since been replaced by the Charities Act 2011, but according to the Charity Commission, ‘The 2011 Act is intended to make the law easier to understand by replacing four Acts of Parliament with one. It doesn’t make any changes to the law.’ Non-charitable purpose trusts are the subject of the next chapter.

ESSENTIAL READING

- Penner, Chapter 13: ‘Charitable trusts’.

LEARNING OUTCOMES

By the end of this chapter and the relevant readings you should be able to:

- differentiate between purposes that are prima facie charitable and those which are not
- explain how a prima facie charitable object might nevertheless be disqualified from charitable status
- explain what the ‘public benefit’ requirement amounts to
- explain the requirement that a valid charitable trust must be exclusively charitable, and discuss the typical sorts of factors which may prevent its being so
- explain the operation of the cy-près doctrine
- outline why particular areas of charities law raised calls for reform, and the advantages and disadvantages of the enacted reforms.
10.1 Charitable status

10.1.1 A benefit to society

Purpose trusts have for centuries been an important vehicle by which charitable works are carried out. However, it is important to realise that charitable work does not depend on the use of trusts. Most large charitable organisations, such as universities, operate as corporations, not trusts. Most of the law you will study in this chapter will be the law of charity as it applies to all kinds of charitable organisations. In particular, you will be trying to grasp what the law regards as a charitable purpose. Because charitable works are regarded as beneficial to society as a whole, a distribution of funds or an ongoing activity that counts as charitable is typically given preferential treatment under the law, especially in terms of the payment of taxes. For this reason, determining whether a purpose counts as charitable is extremely significant.

10.1.2 Relaxation of trust rules to benefit charities

A number of rules affecting the validity of a trust are relaxed in the case of trusts for exclusively charitable objects:

The beneficiary principle

A charitable trust has no beneficiaries. This is true even where the individuals who in fact benefit from the trust are clearly ascertainable, say in the case of a residential home for the blind. The residents of the home are not beneficiaries of the trust in any legal sense, so they could not enforce the trust nor could they call for a transfer of the trust rights under the *Saunders v Vautier* principle. That trust, like all charitable trusts, can only be enforced by the Charity Commission, which acts on behalf of the Crown: Charities Act 2011, s.13(3). You should bear this point in mind in the discussion of *Re Denley’s Trust Deed* [1969] 1 Ch 373 in the next chapter.

Certainty of objects

The requirement of certainty is relaxed in the case of a charitable trust in the following sense: so long as it is clear that the settlor intended to devote funds to charity, it matters not whether the particular charitable purposes the settlor intended are clearly defined; the court will devise a scheme for the charitable use of the funds. So, for example, a trust simply ‘for charitable purposes’ would be perfectly valid.

The rule against perpetual duration

A charitable trust may last forever. Where charitable trust funds remain, but the particular charitable purpose can no longer practically be carried out, the *cy-près* doctrine will be applied to determine a new, workable, charitable purpose for the funds (see Section 10.5 below).

The rule against remoteness of vesting

This rule does not apply to a gift over from one charity to another. For example, a charitable trust established for a particular residential home for the blind ‘so long as it is situated in Tavistock Square’, and then to the Royal National Institute for the Blind, the shift of funds to the RNIB will be perfectly valid whenever the defeating condition (i.e. the home no longer being located in Tavistock Square) occurs.

The rules of taxation

There are substantial fiscal advantages, in the form of reduction or exemption from various taxes and charges. The details of these tax advantages need not be known, but one should recognise their practical importance to the particular charities and the wider issues raised by this form of tax relief for any purpose falling within the legal definition of charity. There is no agreement amongst the judiciary whether issues of taxation should inform their decision as to what purposes count as charitable.
With the broad scope of charity currently in place, there may be a concern that not all charitable purposes are equally deserving of the fiscal advantages that charitable status confers. There have been suggestions that special tax privileges for charities should be abolished and replaced by direct government grants to those charities which serve more important or vital public services. The chief concern with this idea is that it would reduce the independence of charities from the government of the day, causing them to tailor their activities to please the government; it would also inevitably involve charities devoting a greater portion of their funds and time to political activity, such as lobbying for grants.

**ESSENTIAL READING**
- Charities Act 2011, ss.13–16, 84, 85.

At least one of the following:
- Pettit, Chapter 13: ‘Charitable trusts’, Section 1 ‘Difference between charitable and non-charitable trusts’.

**FURTHER READING**
- Hayton & Mitchell, Chapter 6: ‘Charitable trusts’, Section 1 ‘Legal forms used by charities’ and Section 2 ‘The advantages of charitable status’.

**ACTIVITY 10.1**
Look again at the four ways in which charitable trusts have special status, and write brief summaries of each.
No feedback provided.

**ACTIVITY 10.2**
Based on your reading and your general sense of politics and what counts as a public good, write a brief essay (three or four hundred words) discussing:

a. Why does the state allow fiscal privileges to charities?

b. Given the existence of fiscal privileges, is it appropriate for courts to determine, without the benefit of a statute, which private bodies should receive relief from normal taxation?

c. If fiscal privileges were withdrawn, should the courts be prepared to widen the category of valid purpose trusts?

**10.2 The meaning of ‘charity’**

**ESSENTIAL READING**
Note: this is one of the few sections in this guide where this Essential reading should be looked at before you go on to the succeeding sections.
- Charities Act 2011, ss.1–6.

At least one of the following:
- Oakley, Chapter 11: ‘Charitable trusts’, Section III ‘The definition of charity’.
- Pettit, Chapter 13: ‘Charitable trusts’.


10.2.1 Charitable purposes

Whether a particular purpose is charitable or not is a question of considerable difficulty, and one which students can find very confusing. The best way to approach the issue is in two stages, asking the following questions:

- Is the purpose *prima facie* charitable?
- If so, is it for the benefit of the public?

These questions are now on a statutory footing in s.2(1) of the Charities Act 2011. The first is considered here and the second in Sections 10.3 and 10.4 below.

We begin with the first question. Is the purpose *prima facie* charitable? Prior to the Charities Act 2006 (now 2011) an important factor in determining whether a purpose was charitable was whether it fell within the wording of the Preamble to the Statute of Charitable Uses 1601, which provided as follows:

\[
\text{Whereas lands, tenements, rents, annuities, profits, hereditaments, goods, chattels, money and stocks of money have been heretofore given, limited, appointed and assigned, as well by the Queen's most excellent majesty, and her most noble progenitors, as by sundry other well disposed persons; some for the relief of aged, impotent and poor People, some for Maintenance of sick and maimed soldiers and Mariners, Schools of Learning, Ports, Havens, Causeways, Churches, Sea-Banks and Highways, some for Education and Preferment of Orphans, some for or towards the Relief, Stock or Maintenance of Houses of Correction, some for Marriages of poor maids, some for Supportation, Aid and help of Young Tradesmen, of Prisoners or Captives, and for Aid or Ease of any poor Inhabitants concerning payments of Fifteens, setting out Soldiers and other Taxes; which Lands, Tenements, Rents, Annuities, Profits, Hereditaments, Goods, Chattels, Money and Stocks of Money, nevertheless have not been employed according to the charitable intent of the givers and founders thereof, by reason of frauds, Breaches of trust and Negligence in those that should pay, deliver and employ the same.}
\]

In *Income Tax Commissioners v Pemsel* (1891), Lord Macnaghten distilled the preamble down to four categories:

a. trusts for the relief of poverty
b. trusts for the advancement of education
c. trusts for the advancement of religion
d. trusts for other purposes within the ‘spirit and intendment of the preamble’.

The most difficult head of charity – because it is the hardest to define – is the last. It is not enough simply to show that the purpose confers a benefit on the public – it must also be shown that the benefit conferred is within the spirit and intendment of the preamble: see *Williams v IRC* (1947).

Under the Charities Act 2011, s.3(1), these four heads are now 13 heads. There have been some new additions, but most of the extra nine were pulled out of Lord Macnaghten’s residual fourth category (leaving a smaller residue still working on the same basic principle):

a. the prevention or relief of poverty
b. the advancement of education  
c. the advancement of religion  
d. the advancement of health or the saving of lives  
e. the advancement of citizenship or community development  
f. the advancement of the arts, culture, heritage or science  
g. the advancement of amateur sport  
h. the advancement of human rights, conflict resolution or reconciliation or the promotion of religious or racial harmony or equality and diversity  
i. the advancement of environmental protection or improvement  
j. the relief of those in need because of youth, age, ill-health, disability, financial hardship or other disadvantage  
k. the advancement of animal welfare  
l. the promotion of the efficiency of the armed forces of the Crown or of the efficiency of the police, fire and rescue services or ambulance services  
m. any other purposes—  
   i. that are not within paragraphs (a) to (l) but are recognised as charitable purposes by virtue of section 5 (recreational and similar trusts, etc.) or under the old law  
   ii. that may reasonably be regarded as analogous to, or within the spirit of, any purposes falling within any of paragraphs (a) to (l) or sub-paragraph (i), or  
   iii. that may reasonably be regarded as analogous to, or within the spirit of, any purposes which have been recognised, under the law relating to charities in England and Wales, as falling within sub-paragraph (ii) or this sub-paragraph.

10.2.2 The prevention or relief of poverty

Trusts for the relief of poverty provide for those who are deprived of a reasonable standard of living. The intended recipients do not have to be destitute. The recipients do actually have to be poor, however, so in Re Scarisbrook [1951] Ch 622, a trust for an individual’s ‘poor relations’ was charitable, but in Re Sander’s WT [1954] The Times 22 July, one for the ‘working classes’ was not charitable because not all those in ‘the working class’ are poor.

The Charities Act 2011, s.3(1)(a) adds ‘prevention’ to the traditional head of relief of poverty. This was considered by the Upper Tribunal (Tax and Chancery Chamber) in Charity Commission for England and Wales v A-G [2012] UKUT B19 (TCC), [75]:

[T]he prevention of poverty entails addressing the causes of poverty, while relief entails addressing the consequences of poverty. The prevention of poverty is recognised by section [3](1)(a) as a stand-alone purpose which can be pursued, for example, by charities which provide money management advice... [W]e know of no authority which has considered trusts for the prevention of poverty.

This case is discussed further below in connection with the public benefit requirement.

Activity 10.3

Read Re Niyazi’s WT [1978] 1 WLR 910 and explain why Megarry V-C thought the facts were ‘desperately near the borderline’.

10.2.3 The advancement of education

Traditional forms of education and training clearly fall under this head, so trusts for schools, colleges, universities and so on are valid. ‘Education’, however, is much broader, covering research, the dissemination of useful knowledge (Incorporated Council of Law Reporting v A-G [1972] Ch 73), artistic education (Royal Choral Society v IRC [1943] 2 All ER
101), museums (British Museum Trustees v White (1826) 2 Sim & St 594), the promotion of culture (Re Delius [1957] Ch 299), school sports facilities (Re Mariette [1915] 2 Ch 284), and activities associated with education such as student unions (London Hospital Medical College v IRC [1976] 1 WLR 613) and professional bodies that advance education (Royal College of Surgeons of England v National Provincial Bank Ltd [1952] AC 631).

However, while courts are careful to ensure that this head is not used to provide charitable status for political purposes masquerading as education such as the production and publication of propaganda or party political literature (Re Hopkinson [1949] 1 All ER 346), the mere fact that research, education, or the dissemination of knowledge concerns politically controversial issues does not disqualify it from charitable status (Re Koeppler WT [1986] Ch 423).

**Activity 10.4**

In his will, the famous writer George Bernard Shaw left money on trust for research into the development of a 40-letter alphabet for English. Do you think the trust was a valid charitable trust? Read Re Shaw [1957] 1 WLR 729 for the answer, and then read Re Hopkins’ WT [1965] Ch 699. Were the decisions in these cases correct?

**10.2.4 The advancement of religion**

Religion comprises all the variety of religions human beings practise – the law takes the general view that any religion is better than none, but is neutral as between them (see Neville Estates Ltd v Madden [1962] Ch 832). But trusts for the promotion of ethical behaviour without a component of spiritual belief are not trusts for the advancement of religion (Re South Place Ethical Society [1980] 1 WLR 1565), though such trusts may be charitable under the fourth head of charity.

The Charities Act 2011, s.3(2)(a) now provides that

‘religion’ includes—

(i) a religion which involves belief in more than one god, and

(ii) a religion which does not involve belief in a god.

This confirms that faiths with multiple deities (e.g. Hinduism) or with no deities (e.g. Buddhism) are included in the definition of religion. In R (Hodkin) v Registrar-General of Births, Deaths and Marriages [2013] UKSC 77, [2014] 2 WLR 23, the Supreme Court decided that the Church of Scientology in London was a ‘place of meeting for religious worship’ within the meaning of s.2 of the Places of Worship Registration Act 1855, and therefore it could be used for marriage ceremonies. The court decided that Scientology was a religion within the meaning of s.3(2)(a) of the Charities Act 2011. This was not a decision concerning its status as a charity. Previously, the Charity Commission had decided that Scientology was not a religion for the purposes of English charity law, but this was before the new definition of religion in the 2006 Act. However, the Commission had also decided that the church was not established for the public benefit.

**Activity 10.5**

Consider whether a movement which claims that its members are able to ‘raise their consciousness and realise their place in the Universe’ by ‘getting in touch with their inner child’ is a religion under charity law. Then read R v Registrar General, ex p Segerdal [1970] 2 QB 697 and see if you would change your mind.

No feedback provided.

**10.2.5 Other purposes beneficial to the community**

This was always the most difficult category on which to set coherent boundaries, and it is here that reference was most often made to the Preamble of the 1601 Act. The essential point to grasp is that a trust is not charitable merely because it benefits some section of the public. As Viscount Cave said in A-G v National Provincial and Union Bank of England [1924] AC 262, ‘it is not enough to say that the trust in question is for public purposes beneficial to the community; you must also show it to be a charitable trust’.
It must be for the public benefit in a way which can be related to the purposes set out in the Preamble or to purposes which later courts have found to be analogous to those in the Preamble.

The ‘relief of aged, impotent and poor’ people was construed disjunctively; that is, a charity can be for the aged or the impotent or the poor and be valid – it need not be for people with all three misfortunes. ‘Impotent’ provided an explicit basis for trusts for the disabled (Re Lewis [1955] Ch 104; Re Fraser (1883) 22 Ch D 827), and for trusts for hospitals generally. These purposes continue under the Charities Act 2011, s.3(1)(d) and (j):

(d) the advancement of health or the saving of lives;
(j) the relief of those in need because of youth, age, ill-health, disability, financial hardship or other disadvantage.

Trusts for disaster relief are problematic. While trusts for the relief of victims of disasters are charitable (Re North Devon and West Somerset Relief Fund Trusts [1953] 1 WLR 1260), they are so only to the extent they provide benefits to the ill or disabled, relieve victims of poverty or fall under another recognised head of charity (e.g. rebuilding a school or church). The Charity Commission strongly encourages people to donate to, or work with existing charities rather than creating a new charity to respond to a particular disaster: see Charity Commission guidance on starting, running and supporting charitable disaster appeals (CC40).

While trusts related to school activities are charitable under the education head, trusts for sport or recreation outside of the education context are not (Re Nottage [1895] 2 Ch 649). However, the provision of public facilities which can be used for recreation is charitable (Re Hadden [1932] 1 Ch 133). This is now governed by the Charities Act 2011, s.5. It does not matter if the rich benefit from the recreational facility as well as the poor or deprived, so long as it is genuinely open to all members of the public, although it can be restricted to male or female only.

The Charities Act 2011, s.3(1) now includes ‘(e) the advancement of citizenship or community development’, ‘(g) the advancement of amateur sport’, ‘(h) the advancement of human rights’ and ‘(k) the advancement of animal welfare’. Would Williams Trustees v IRC (1947) now count as charitable? Would McGovern v A-G (1982) now be charitable, or would the fact that it purported to operate overseas still be problematic?

In Incorporated Council of Law Reporting for England and Wales v A-G (1971), the Court of Appeal decided that the publication of law reports at a moderate price was a valid charitable purpose for the advancement of education, but also under the residual category as purpose ‘of general public utility’, since it was necessary for the proper administration of justice, like a public court house. The concept ‘of general public utility’ was considered by the Court of Appeal in Helena Partnerships Ltd v HMRC (2012), where it decided that the provision of social housing did not qualify (per Lloyd LJ at [108]):

In its nature, the benefit afforded by the provision of housing to the person who is thereby housed is of an altogether different order, as it seems to me, to the benefit afforded by the construction or maintenance of a road, a bridge or a sea-wall, or the maintenance of a fire brigade or a lifeboat service. The former provides direct benefits to the occupants of the accommodation which far outweigh the degree of indirect benefit that other members of the community may derive from the existence of the housing stock.

If the housing had been provided only to disadvantaged people in need of relief, due to poverty, old age, infirmity, etc., it would have qualified as charitable, but without such a restriction, it was not.
Activity 10.6
Consider whether each of the following purposes is charitable, read the case following to see how your views compare with those of the courts, and then consider how the Charities Act 2011 might apply.

a. A gift on trust to establish and maintain an institute, to be known as the ‘London Welsh Association’, the purposes of which included maintaining an institute for the benefit of Welsh people in London, and promoting their language and culture (Williams’ Trustees v IRC [1947] UKHL 1, [1947] AC 447).

b. The work of the National Trust for Places of Historic Interest or Natural Beauty (Re Verrall [1916] 1 Ch 100).

c. The work of the Society for the Prevention of Cruelty to Animals (Thatam v Drummond (1864) 2 Hem & M 262).

d. A gift for an animal sanctuary which specifically excluded humans so that the animals would not be molested (Re Grove-Grady [1929] 1 Ch 557).

e. A trust for the purpose of promoting athletic sports and general pastimes for the Glasgow police (IRC v City of Glasgow Police Athletic Association [1953] AC 380).

f. The provision of facilities for religious services and instruction and for the social and physical training and recreation of persons who would otherwise be deprived of these services and who were or were likely to become members of the Methodist Church (IRC v Baddeley [1955] UKHL 1, [1955] AC 572).

No feedback provided.

Summary
There is a two-stage test to determine whether a particular purpose is charitable. Is the purpose prima facie charitable and if so, does it provide a public benefit?

There are 13 main categories of charity under the Charities Act 2011, which build on the four categories set out by Lord Macnaghten in Pemsel (1891). There remains a residual category of other purposes beneficial to the community which is still difficult to define. Essentially, a purpose must benefit the public in a way which can be related to the purposes which later courts have found to be analogous to those in the preamble.

10.3 The public benefit requirement
We need to distinguish between abstract benefit and actual benefit. A charitable purpose must be beneficial to the public, not detrimental. So far as the first three heads are concerned, it was often said to be a ‘presumption’ of public benefit. What seems to be meant by this is that it need not be shown how the particular purpose benefits the public, provided only that there is a sufficient element of the public who are ‘benefited’. So, for example, in a trust for the saying of masses in public, it need not be shown how the public who attend such masses, or those who are edified by knowing that others do so, are benefited by that activity. If there was such a presumption, it appears to have been removed by the Charities Act 2011, s.4(2):

In determining whether the public benefit requirement is satisfied in relation to any purpose falling within section 3(1), it is not to be presumed that a purpose of a particular description is for the public benefit.

In Independent Schools Council v Charity Commission [2011] UKUT 421 (TCC), [2012] Ch 214, the Upper Tribunal decided that there was no presumption of public benefit in relation to education and therefore the statute did not change the law. In Charity Commission for England and Wales v A-G [2012] UKUT B19 (TCC), [39], it came to the same conclusion regarding trusts for the relief of poverty. However, in Catholic Care (Diocese of Leeds) v Charity Commission [2010] EWHC 520 (Ch), [67], Briggs J suggested that the statutory provision might have some effect:
In any event, there was never any such ‘presumption’ in relation to Lord Macnaghten’s fourth category, where it must be shown how the proposed charity will actually benefit the public. In such cases, the balance of benefit against detriment may be an issue. Thus, in *National Anti-Vivisection Society v IRC* (1947), the House of Lords held it imperative to decide whether the benefits to human beings of suppressing vivisection outweighed the benefits to medical science and research that depended on it. (See also *Re Foveaux* [1895] 2 Ch 501 where the court preferred to offer no opinion on the public benefit of abolishing vivisection.)

All four heads, however, are subject to the requirement that it be shown that a section of the public receives the ‘benefit’, and no ‘presumptions’ operate here. That said this requirement seems to be non-existent when it comes to trusts for the relief of poverty. A trust for one’s poor relations is valid (*Re Scarisbrick* (1951)) even though only a private class in fact benefits. In *Charity Commission for England and Wales v A-G* [2012] UKUT B19 (TCC), the Upper Tribunal decided that the Charities Act 2006 (now 2011) had no effect on this aspect of the law, so that trusts for the relief of poverty is still capable of being charitable even though it is limited by relationships based on family, employment or membership in a unincorporated association.

Concerning the advancement of religion, in *Neville Estates Ltd v Madden* (1962) the court said it would assume that ‘some benefit accrues to the public from the attendance at places of worship of persons who live in this world and mix with their fellow citizens.’ However, if there is no engagement with the public, for example in the case of a contemplative order of nuns, there is no public benefit (*Gilmour v Coats* [1949] UKHL 1, [1949] AC 426).

Previously, it was assumed that fee-charging schools and hospitals were charitable, even though only those who can afford the fees can use them, so long as they are not profit-distributing. The Upper Tribunal decided in *Independent Schools Council v Charity Commission* (2011) that a trust that excludes the poor would lack the necessary public benefit to be charitable. This is due to its restriction on public access and not about the relief to poverty. Trusts for the education of children of one locality, such as university scholarships for children of Yorkshire, are valid. However, trusts restricted to children of a family or particular company are not, in particular where the ‘educational trust’ really amounts to a fringe benefit for employees (*Re Koettgen’s WT* [1954] Ch 252; *IRC v Educational Grants Association Ltd* [1967] Ch 993), though this requirement gives rise to some difficult decisions for the courts (e.g. *Oppenheim v Tobacco Securities Trust Co Ltd* [1951] AC 297).

**Activity 10.7**

Consider whether the following meet the ‘public benefit’ requirement, and then read the relevant cases to see if the law agrees with you:

a. A gift to train spiritual mediums (*Re Hummeltenberg* [1923] 1 Ch 237).


No feedback provided.
10.4 Contaminating non-charitable elements

An otherwise valid charitable trust may fail because it contains one of a number of ‘contaminating’ elements.

Politics

Political purposes are not charitable.

ACTIVITY 10.8


1. What reasons do the courts give for denying charitable status to political purposes?
2. Are such reasons persuasive?
3. In what sort of limited political activities are charities allowed to engage?

No feedback provided.

Profit making/profit distribution

Charities may charge for the benefits they confer, as in the case of private hospitals and non-state schools, and charities may engage in fund-raising activities which themselves make a profit, so long as the profit is turned to the charities’ purposes and not distributed to private individuals.

10.5 Failure of charitable trusts: the cy-près doctrine

Cy-près is an Old French legal term meaning ‘as near as possible’. Where a valid charitable purpose would fail because the means chosen by a testator for carrying it out are impractical or impossible, the court will apply the judicially developed cy-près doctrine, and more recently, ss.62 and 67 of the Charities Act 2011. These powers allow the court to order the trust fund to be applied to a different but similar purpose.

It must be noted that the cy-près doctrine is only available where the original trust is for a valid charitable purpose. Do not make the common mistake of thinking that where a purpose trust is invalid because it is not charitable (e.g. because it is for a political purpose) the court may then apply the cy-près doctrine and devote the funds in question to some valid charitable purpose. In such cases there is no charitable trust at all, and the funds will be held on resulting trust for the settlor.

The first issue to determine is whether the trust has truly failed, for it is only then that cy-près may be invoked. If failure has occurred, it is then necessary to decide when that failure occurred. If it was an initial failure, the rights will go on resulting trust unless the donor had a general, or paramount, charitable intention. In the case of subsequent failure (i.e. once rights have been ‘dedicated to charity’), cy-près is available regardless of the presence or absence of any ‘general charitable intent’. Cy-près does not apply if there was a specific gift over to take effect in the event of failure of the gift to charity.

ESSENTIAL READING

- Charities Act 2011, ss.61, 62, 67.
- At least one of the following:
  - Oakley, Chapter 11: ‘Charitable trusts’, Section IV ‘The cy-près doctrine’.
  - Pettit, Chapter 14: ‘The administration of charities’, Section 8 ‘The cy-près doctrine’.
FURTHER READING

ACTIVITY 10.9
Bill dies, leaving by his will funds on trust ‘for the Bermondsey Home for the Aged’. Consider what should happen to the funds in the following situations:

a. There never existed a Bermondsey Home for the Aged or any similarly named institution

b. A Bermondsey Home for the Aged existed until 1991, but its work was taken over by the local NHS hospital

c. The Bermondsey Home for the Aged is the name of a charitable company which no longer operates a home but provides care in the community for the elderly.

Read *Re Faraker* (1912), *Re Vernon’s Will Trusts* (1972), *Re Finger’s Will Trusts* (1972), *Re Spence* (1979) and *Re ARMS (Multiple Sclerosis Research) Ltd* (1997) and *Re Harwood* (1936) to see how the law deals with these cases.

ACTIVITY 10.10
Are the following trust purposes charitable under the present law, and if so, under what head?

a. ‘To finance opposition to a proposed motorway through the Peak District which I regard as an area of outstanding beauty.’

b. ‘To support the public school education of children of employees of the British Steel Corporation, with preference to families in needy circumstances.’

c. ‘To support a Marxist association in its research designed to prove that God does not exist and in campaigning against religion.’

d. ‘To the research unit of the Conservative Party for the advancement of learning in economic policy and electoral reform.’

e. ‘To finance the provision of new squash courts at London University that are to be open for use by members of the local police force as well as by members of the university.’

f. ‘To provide refurbishment funds for the Our Lady of Forest Hill Hospital’ (a private hospital that is run by a religious order and charges fees).

g. ‘At such times and in such manner as my trustees in their absolute discretion think fit for the benefit of any of my relatives who, in the opinion of my trustees, lack ordinary comforts.’

h. ‘To campaign for the abolition of torture, capital punishment and corporal punishment.’

SELF-ASSESSMENT QUESTIONS
1. Who, if anyone, is the beneficiary of a charitable trust to, say, ‘educate children in the principles of Buddhism’?

2. Who, if anyone, can enforce a charitable trust?

3. What is the ‘cy-près’ doctrine?

4. When can the ‘cy-près’ doctrine be invoked?

5. Lord Macnaghten identified four categories of valid purposes for charitable trusts. What are they?

6. Which of the 13 categories in the Charities Act 2011, s.3(1) were not previously contained in Lord Macnaghten’s four categories?

7. In what circumstances can the provision of facilities for sport and recreation be considered charitable?
8. What problem may arise with charitable trusts for ‘disaster relief’?

9. What might be the disadvantages of replacing tax reliefs for charities with direct government grants?

SAMPLE EXAMINATION QUESTIONS

Question 1  Answer both parts

a. On what basis does the law determine whether a proposed trust, which appears to provide for a novel purpose (i.e. one not found to be either charitable or uncharitable by a previous judicial decision) is charitable? Are any reforms of the law indicated?

b. Siegfried died, leaving in his will ‘£50,000 to the Stepney Grammar School for scholarships to deserving boys’ and ‘£50,000 for the work of “Stepney Food for the Homeless”’. Stepney Grammar School, though it previously had only male pupils, is now mixed, and the current board of governors has advised the trustees that they would not administer a scholarship scheme for boys only. Stepney Food for the Homeless was a corporate charitable body which has since been wound up. Its work, however, was continued and is now carried on by East London Food for the Homeless. Advise the trustees.

Question 2  Consider four of the following six purposes, and discuss whether they are charitable in English law, and if not, whether they ought to be:

a. To provide scholarships to assist students to learn ballroom dancing while at university, with the condition that the trustees may, in applying up to 75 per cent of the income of the trust, give preference to children of employees of Capezio Ltd.

b. To campaign for a modern national health service in Erehwon, a country plagued by poverty and disease, where there are strong religious objections to medical procedures which involve any invasion of the body, such as surgery or vaccination by syringe.

c. To support the work of Osiris, a cult whose way of life and philosophy is based on an interpretation of ancient Egyptian supernatural beliefs, and whose doctrines require adherents to cut themselves off entirely from their families and retire to Osirian communities, where they make themselves available several times each month to discuss their faith with members of the public.

d. To provide funds to the Sisters of 2001, an association of Roman Catholic nuns whose sole activity is to persuade the Vatican to allow the ordination of women priests.

e. ‘£10 million to my trustees upon trust for the purpose of setting up an Olympic Sporting Institute, for the better training of Great Britain’s most promising young amateur athletes.’

f. ‘£1 million for the provision of condoms and other means of birth control to students in schools in London.’

Question 3  What is the ‘public benefit’ requirement? How, if at all, does it vary across the range of charitable purposes?

Question 4  Answer both parts:

a. ‘Despite the enactment of the Charities Act 2011, the present definition of charity is still in need of reform because we must still rely on analogies that are haphazard and capricious. The statutory list should exclude purposes that are not genuinely altruistic, redistributive and socially useful.’

b. ‘It is of course unfortunate that the recognition of any trust as a valid charitable trust should automatically confer fiscal privileges, for the question whether a trust to further some purpose is so little likely to benefit the public that it ought to be declared invalid and the question whether it is likely to confer such great
benefits on the public that it should enjoy fiscal immunity are really two quite
different questions’ (per Lord Cross in Dingle v Turner (1972)).
Discuss.

ADVICE ON ANSWERING THE QUESTIONS

Question 1

a. An answer to this question will explain the ‘growth by analogy’ approach to novel
purposes seen in Scottish Burial Reform and Cremation Society v Glasgow Corp
(1968) and will compare it with the more broad-ranging ‘public benefit’ approach
Students should consider possible reforms such as the provision of a statutory
definition of charity, and consider both the advantages and disadvantages of
particular proposed reforms.

b. These are cases of impracticality or impossibility of performance of a charitable
purpose at the outset and the possible application of the cy-près doctrine. The
student should consider how the court would assess whether the apparent
intention of the testator to determine whether the gift of scholarships to boys is an
essential element of the gift, and whether the court could apply the funds cy-près
to allow the fund to be used for scholarships for girls as well as boys. Consideration
of Re Lysaght (1966) is essential. The second concerns the case of a charitable
institution whose work is continued by another. Normally, the funds will be
transferred to the continuing body, but this is not a case of cy-près – see Re Farakar
(1912).

Question 2

a. While learning ballroom dancing may not appear to be particularly educational,
such an activity could easily be regarded as ancillary to university education, and
therefore a charitable purpose. However, the preference may well render the trust
non-charitable (Re Koettgen’s WT (1954), IRC v Educational Grants Association Ltd
(1967)).

b. This would probably fail to be a valid charitable purpose, being tainted by politics
under McGovern v A-G (1982) principles, even though the provision of healthcare in
a poor country would count as charitable.

c. Whether Osiris’s work is charitable under the head of religion will depend upon
whether their way of life is ‘religious’, involving belief in a higher power, or merely
moral or philosophical (Re South Place Ethical Society (1980), R v Registrar-General
(1970)) and whether the extensive isolation of their members removes any public
benefit (Neville Estates v Madden (1962)).

d. While this purpose is situated within a religious context, it is not clear that
the activity is itself religious or a matter of church politics. As the Vatican is
an independent state, the trust may raise some McGovern v A-G (1982) issues
concerning politics. On the other hand, the purpose may be regarded as
educational in the sense that it provides for the discussion of Church doctrine,
although again the dissemination of research or activity which is organised to
promote one side of a debate would appear to fail as charitable research.

e. This concerns the apparent prohibition on trusts for sporting activity not
associated with traditional education (Re Nottage (1895), the Birchfield Harriers
decision by the Charities Commissioners (Annual Report, 1989); this might appear
unjustifiable if there is a public interest in Britain’s achieving international sporting
excellence; one might try to fit the ‘training of Britain’s most promising young
athletes’ under the education head, but this may seem somewhat strained given
that the proposed institute is independent of any regular educational institution;
the trust will not be validated under the Recreational Charities Act 1958, since this
institute will not serve social welfare by improving the conditions of life of the
athletes, and is not open to the public.
f. Concerns public benefit and possible public detriment; sex education might be education, but the mere provision of means of birth control is not; it might advance the health of students to the extent unwanted pregnancies and sexually transmitted diseases are avoided; however, some might regard it as encouraging sex amongst the young, which is not universally regarded as beneficial.

**Question 3**  This question is straightforward, requiring the student to discuss how the requirement applies to cases under each of the heads of charity, and in particular a student must discuss how the requirement may appear artificial in the case of religious charities and becomes problematic in the case of educational charities and charities under the fourth head when cases concerning employee ‘fringe benefits’ and fee-charging charities arise.

**Question 4**  Another straightforward question concerning the reform of charities, (a) being directed to the definition of charities, (b) regarding the automatic fiscal benefits accorded to charity. With regard to (a), criticisms of the current scope of charities should be identified and explained, and proposals for reform discussed. In particular, the difficulties in formulating a satisfactory statutory definition should be addressed, as well as any problems that might arise (e.g. the rendering non-charitable of long-standing charities). As to (b), Lord Cross’s suggestion that fiscal benefit and charitable status be decoupled is a common one. A good answer would consider not only the reasons why it has often been thought a good way forward, but how a new regime of tax subsidy, or direct government grants might be structured, and the advantages and possible drawbacks of particular reforms.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>Topic</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can differentiate between purposes that are <em>prima facie</em> charitable and those which are not.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>I can explain how a <em>prima facie</em> charitable object might nevertheless be disqualified from charitable status.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>I can explain what the ‘public benefit’ requirement amounts to.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>I can explain the requirement that a valid charitable trust must be exclusively charitable, and discuss the typical sorts of factors which may prevent its being so.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>I can explain the operation of the <em>cy-près</em> doctrine.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>I can outline why particular areas of charities law raised calls for reform, and the advantages and disadvantages of the enacted reforms.</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>10.1 Charitable status</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>10.2 The meaning of ‘charity’</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>10.3 The public benefit requirement</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>10.4 Contaminating non-charitable elements</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>10.5 Failure of charitable trusts: the <em>cy-près</em> doctrine</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
</tbody>
</table>
11 Purpose trusts II: private purposes

Contents

Introduction .............................................................. 120

11.1 Objections to private purpose trusts ...................... 121

11.2 The ‘beneficiary principle’ and the ‘no purpose trust’ rule .... 122

11.3 Trusts for persons limited by a purpose .................... 124

11.4 Anomalous valid private purpose trusts .................... 125

11.5 Departures from the beneficiary principle ................. 126

Reflect and review ..................................................... 128
Introduction

In this chapter we look at the general prohibition upon settlors creating trusts for non-charitable purposes. The law does not frown upon persons spending their money as they see fit on a particular purpose, but finds it impossible to accommodate the dedication of rights to the carrying out of certain purposes within the mechanism of the trust, unless there is someone who can enforce the trust.

As we will see, attempts have been made to circumvent the rule, but a clear understanding of its nature shows how these attempts fail to deliver the intended result. The basic reason for this is simple: there is no one with a right to enforce the trust against the trustee unless there are beneficiaries under the trust (or the trust is for a charitable purpose enforced by the Charity Commissioners). A purpose can neither hold any rights nor enforce them, so a private purpose trust cannot amount to an enforceable trust for a purpose. The work in this chapter builds on that already studied in Chapter 5 and you should reacquaint yourself with that material before attempting that topic.

Essential reading
- Re-read Chapter 5: ‘Creating express trusts I: the declaration of trust’.

Learning outcomes
By the end of this chapter and the relevant readings, you should be able to:
- state the main objections to private purpose trusts
- discuss the interrelationship between the requirement of certainty of objects and the beneficiary principle, and how the beneficiary principle can be seen as a ‘rights’ principle or an ‘enforcement’ principle
- discuss cases in which apparent trusts for purposes were held valid and why this does not upset the beneficiary principle
- describe the few private purpose trusts that will nevertheless be upheld and how they are enforced
- explain why the trust validated in Re Denley’s Trust Deed [1969] 1 Ch 373 might be seen as a problematic example of a private purpose trust.
11.1 Objections to private purpose trusts

Private non-charitable purpose trusts pose difficulties for trusts law because they do not satisfy some of the traditional trust law doctrines. As a result, a trust that requires rights to be used for a designated purpose which is not exclusively charitable may be void on one of a number of grounds.

11.1.1 Uncertainty of objects

A direction to carry out a purpose generally fails to indicate a clear class of individuals who will benefit if it is carried out, and so it is impossible to identify a class of beneficiaries. See, for example, Re Astor's ST [1952] Ch 534; Morice v Bishop of Durham (1804) 9 Ves 399, 32 ER 656 (Grant MR); affirmed [1805] EWHC Ch J80, 10 Ves 522, 32 ER 947 (Eldon LC).

11.1.2 Excessive duration

The rule is generally taken to be that a trust fails if it may last beyond the various perpetuity periods allowed by law. Trusts which require rights to be retained for a period in excess of any valid perpetuity period will clearly infringe the rule, and since purposes generally do not expire within a limited time, they tend to violate the rule: see, for example, MacAulay v O'Donnell [1943] Ch 435. If that is correct, then the rule was applied liberally in Mussett v Bingle [1876] WN 170, where a trust to erect a monument was held not to be perpetuitous, even though there would have been some (remote) possibility that it would take more than the allowable defined period of 21 years to carry out the terms of the trust (see also Re Lipinski's Will Trusts [1976] Ch 235). In practice, a settlor could avoid infringing this rule by specifically stating a period for the operation of the trust within the periods allowed, rather than relying upon the limitless ‘natural’ lifetime of the purpose. According to s.18 of the Perpetuities and Accumulations Act 2009, ‘This Act does not affect the rule of law which limits the duration of non-charitable purpose trusts.’ So the trust would have to comply with the common law rule. However, such a solution to this perpetuity problem does not solve the more fundamental issue of whether private purpose trusts per se are valid at all.

11.1.3 Lack of beneficiary

It is a core feature of the trust that it is enforced against the trustee by the beneficiaries and by no one else (including the settlor). It would therefore seem to follow that any effective trust must have beneficiaries, for only beneficiaries have the ability to enforce it against the trustee. (In the case of charitable or public trusts, the Charity Commission has this power.) This point has been dwelt upon in many cases: see, for example, Re Astor's ST [1952] Ch 534; Re Shaw [1957] 1 WLR 729; [1957] 1 All ER 745; Re Endacott [1960] Ch 232; Leahy v A-G for NSW [1959] UKPC 1, [1959] AC 457. In Re Denley's Trust Deed [1969] 1 Ch 373, this question was reduced by Goff J to one of ‘standing’, holding that the prospect of obtaining some ‘factual benefit’ from the performance of the trust was sufficient. Some think that this is too remote an interest: J. M. Evans (1969) 32 MLR 96. Re Endacott, a decision of the Court of Appeal, on the other hand, holds that it must be possible to point to someone with an equitable interest, and it is difficult to see how Re Endacott and Re Denley can be reconciled.

**Activity 11.1**

Make a short spoken statement outlining the reasons why it is difficult to reconcile Re Endacott and Re Denley.

No feedback provided.

11.1.4 Excessive testamentary delegation

It is sometimes suggested that a testator creating a trust for a non-charitable purpose fails to exercise their testamentary power because they leave it to the trustee to decide whether or not the rights will be so used: see Leahy v A-G for NSW. This objection is insubstantial on its own. If someone with sufficient standing to enforce the trust is available, then the trustee will be under an enforceable duty to carry out the purpose,
whether or not to carry it out will not be a matter for their discretion. Thus this objection begs the question: if purpose trusts are valid, then testamentary purpose trusts will not represent a failure to exercise a testamentary power. If they are invalid, then they will ipso facto be invalid testamentary dispositions. Nothing in particular to do with testamentary dispositions affects the issue.

Clearly, objections 1 (uncertainty of objects) and 3 (lack of beneficiary) are the most crucial, and it is upon these that we will spend most of our time in the remaining sections of this chapter.

**Activity 11.2**

Devise two non-charitable purposes that you would like to see carried out, then list the people or sorts of people who would most likely benefit in fact from their being carried out. State whether those persons:

a. would be likely to take the effort to enforce the purpose against a holder of funds for the purpose

b. should be allowed by law to enforce the purpose

c. should be allowed by law to come to an agreement with the holder of the funds to use the funds for some other purpose or to divide the funds up amongst themselves.

**Summary**

A private purpose trust may be void on a number of grounds. The two most important grounds are (1) uncertainty of objects, as a purpose trust does not clearly indicate a class of beneficiaries, and (2) the absence of any beneficiaries. An effective trust must have at least one beneficiary, as only the beneficiaries have rights enforceable against the trustee. Furthermore, excessive duration may cause a trust to fail, if the trust purpose extends beyond the various perpetuity periods allowed by law.

### 11.2 The ‘beneficiary principle’ and the ‘no purpose trust’ rule

The 'beneficiary principle' states that a valid trust must be for the benefit of ascertainable individuals (i.e. the trust must have beneficiaries). In consequence, the courts will not normally enforce a trust to carry out a private purpose since the benefits of carrying it out are not owed to any specific individuals. Hence, the principle is also framed as the 'no purpose trust' rule.

There can be no trust, over the exercise of which this Court will not assume a control; for an uncontrollable power of disposition would be ownership, and not trust ... There must be somebody, in whose favour the court can decree performance. (*Morice v Bishop of Durham* (1804) per Sir William Grant MR.)

For comparison, consider the privity rule of contract law as it existed before the statutory reforms in 1999. Only parties to a contract could enforce it. Even if some third party might benefit from the performance of a contract, that alone gave the party no interest under the contract, and thus no right to enforce it.

#### 11.2.1 A ‘rights’ principle or an ‘enforcer’ principle?

The beneficiary principle can, from one perspective, be seen as a corollary of the certainty of objects required for a valid declaration of trust. If a declaration of trust expresses the trustee's distributive duties in terms of a purpose, then clearly there are no definite trust objects.

Further, since the execution of a trust must be under the control of the court,

it must be of such a nature, that it can be under that control; ... unless the subject and the objects can be ascertained, upon principles, familiar in other cases, it must be decided, that the court can neither reform maladministration, nor direct a due administration. (*Morice v Bishop of Durham* (1805) per Lord Eldon LC).
Compare the following statement by Roxburgh J in Re Astor's ST (1952):

The typical case of a trust is one in which the legal owner of property is constrained by a court of equity so to deal with it as to give effect to the equitable right of another. These equitable rights have been hammered out in the process of litigation in which a claimant on equitable grounds has successfully asserted rights against a legal owner or other person in control of property. Prima facie, therefore, a trustee would not be expected to be subject to an equitable obligation unless there was somebody who could enforce a correlative equitable right, and the nature and extent of that obligation would be worked out in proceedings for enforcement.

This passage states that a right-holder is either under an equitable duty or is not, and if they are, then someone else must have corresponding equitable rights which can be enforced against the right-holder. If they are not under an equitable duty, then they can deal with the rights as they wish because they hold them outright.

**Private law and outright holding**

Together, these two passages express the beneficiary principle as a ‘rights’ principle: if there is no one with rights against the trustee, then there is no one who can enforce the trust and thus no trust. The problem with purpose trusts, on this view, is simply that expressing a trust in terms of a purpose confers no rights upon anyone in equity. Trusts (except for charitable trusts) are devices of private law after all, and for a private law transaction of whatever kind to have any legal effect, it must actually confer rights or powers, with corresponding duties or liabilities. Dedicating rights to a purpose does neither.

However, some commentators have attempted to distinguish two aspects of the role of beneficiaries: first, they have equitable interests in the trust assets, and second, they have standing to enforce the trust. Of course, where a trust is for ascertainable beneficiaries, they should, for the most part, be the proper enforcers of their own rights. But why should a court of equity not validate a trust for beneficiaries where the settlor has nominated someone else to serve as the enforcer of those beneficiaries’ rights? If this seems workable, why should a court of equity not validate a trust for a private, non-charitable purpose, where the settlor has nominated an enforcer, who can take the trustees to court if they fail to carry it out? On this reasoning, the ‘beneficiary principle’ should be regarded as an ‘enforcer principle’, and would state that a trust is only invalid where there is no one with standing to enforce the trust, either beneficiaries or nominated enforcers. Arguably, *Re Denley* (below, Section 11.5) implicitly adopts that approach.

**Is there a duty to enforce?**

The problem raised by such an approach becomes obvious upon a little thought, so long as you keep in mind the point that trusts are arrangements of private law. The state has no interest in seeing trusts for private purposes enforced. Whether enforcement, or something else, occurs following the validation of these trusts by the court is a matter of the private rights of individuals. Remember that beneficiaries under a trust have no duty to enforce their rights against the trustee. The state does not require them to see that the trustee gives them any proper distributions under the terms of the trust. Indeed, beneficiaries can release them, or can assign them to the trustee if they are so minded (though the trustee will have the burden of showing that such an assignment was fairly and freely entered into). This ethos, that it is up to individuals themselves to enforce their private rights, must apply equally to the person nominated ‘enforcer’ of the purpose trust. If that person chooses not to enforce the trust against the trustee, or release their rights of enforcement, the state will not step in. And if that person comes to an agreement with the trustee to use the rights in other ways, or divide them up between themselves, this would be perfectly lawful, for there is no one else whose rights have been infringed.

If this is true, then how is this a trust to carry out a purpose, rather than just a trust with a particular distribution of rights and duties amongst individuals? In some
jurisdictions where legislation has been enacted to permit non-charitable purpose trusts, the enforcer is under a statutory duty to enforce the trust (e.g. Cayman Islands Trust Law (2011 Revision), s.101; The Trusts (Guernsey) Law, 2007, s.12; Trusts (Jersey) Law 1984, s.13). Such enforcers can be regarded as quasi-public officials whose duties are imposed by public law. However, in the absence of such legislation, as in England and Wales, enforcers of private purpose trusts would have no similar public law duties.

**Activity 11.3**

a. What does it mean to say that the beneficiary principle is a ‘rights’ principle rather than an ‘enforcer’ principle?

b. What flaw does there seem to be in the ‘enforcer’ principle in the case of private purpose trusts?

No feedback provided.

**11.2.2 Powers for purposes**

While the orthodox principles of trust law seem to invalidate trusts to carry out private purposes, the grant of a power to a trustee to use trust funds to carry out a purpose appears to be perfectly valid. There is no similar problem of enforcement with respect to powers, for there is no duty to carry out powers and therefore no problem of nonfeasance. Regarding misfeasance, those who would take in default of appointment have the power to bring the trustees to account if they purport to exercise the power in a way which is outside its intended purpose. The court will not, however, validate invalid purpose trusts by construing them as valid powers for purposes: *Re Shaw*.

**Summary**

Private purpose trusts are invalid under English law, but different explanations of why this is so have been offered. The essential problem appears to lie in the fact that unless there are beneficiaries, the right-holder is not bound by any trust. The naming of an enforcer to enforce a purpose trust against the trustee does not solve the problem, for the enforcer can treat their enforcement rights as merely rights they hold for their own benefit, so that they can depart from enforcing the trust and may release their rights or bargain with the trustee for a division of the trust rights. In short, there is no duty to enforce the trust purpose that can bind an enforcer. Powers to carry out purposes are perfectly valid. Here there is no duty on the trustee to exercise the power to carry out the purpose, so no concern to find a mechanism to enforce that duty against the trustee.

**Reflection point**

Is there a case for making private purpose trusts valid in English law?

**11.3 Trusts for persons limited by a purpose**

There is a class of trusts which are often mistaken for true purpose trusts by the unwary. These are trusts like *Re Sanderson’s Trust* (1857) K & J 497, 69 ER 1206, where the beneficiary’s interest under the trust is determined by the expense of a certain benefit for him. So for example, trusts for the maintenance, advancement, or education of sons or daughters were popular in the 19th century. While these trusts are created to fulfil a purpose (e.g. to maintain Emily, advance Frederick or educate Rita), they are not purpose trusts without beneficiaries. Emily has a claim against the trustees for such amounts as are needed for her maintenance, Fred for as much as is needed to, say, buy a commission in the army and Rita for as much as is needed to pay for her education. They are, in other words, trusts for people, in which the subject-matter of the trust for the individual beneficiary is not determined by a straightforward allocation of a share of income or capital, but by the cost or expense of a particular benefit for the beneficiary. For this reason, the trust may exhaust all the funds set aside for it, or may fail to exhaust those funds.
It is often difficult to distinguish a Re Sanderson-type trust from a trust where the intention of the settlor is to give an entire fund to a beneficiary, but the settlor expresses ‘education’ or some other expense as the motive for the gift. A mere expression of motive cannot limit a gift, and so in these latter cases, if the fund provided for the beneficiary is not exhausted by the expressed expense, this is of no matter, for the whole fund was held for the beneficiary from the outset. Where, however, there is a true Re Sanderson-type trust, the beneficiary only has a right under the trust commensurate with the named expense, and any remaining funds must be disposed of by way of a gift over, or will otherwise go on resulting trust. Re Abbott [1900] 2 Ch 326 and Re Andrew [1905] 2 Ch 48 provide an interesting contrast between the two types of case. Both concerned funds raised by public subscription, to provide for two disabled ladies and a cleric’s children, respectively. See also Re Osoba [1978] 1 WLR 791, [1978] 2 All ER 1099; varied [1979] 1 WLR 247, [1979] 2 All ER 393 (CA).

Activity 11.4

a. What sorts of purposes typically defined the extent of a beneficiary’s interest under a Re Sanderson type of trust?

b. Explain why the Re Sanderson type of trust is often difficult to distinguish from a trust of the whole of a fund with an expressed motive for the gift, and the practical difference between the two kinds of trust.

11.4 Anomalous valid private purpose trusts

A number of purpose trusts have been upheld, despite infringing the beneficiary principle, and in Re Dean (1889) 41 Ch D 552, despite also infringing the rule against perpetuities. The categories, which are not to be extended (Re Endacott; Re Astor), are:

- reasonable provision for tombs and monuments (but not something more general, such as ‘some useful memorial to myself’, as in Re Endacott itself)
- the care of specific animals (Re Dean)
- the saying of masses (religious services in the Catholic Church) to the extent that these are not charitable in advancement of religion (Bourne v Keane [1919] AC 815; Re Hetherington [1990] Ch 1).

The furtherance of fox-hunting was included in the list in Re Thompson [1934] Ch 342, but fox-hunting is now illegal in England and Wales: Hunting Act 2004. It should be noted that no real challenge to the validity of the trust was made in that case.

11.4.1 The Pettingall order and ‘trusts of imperfect obligation’

Where an anomalous trust of one of these kinds is upheld, the court will make a Pettingall order (Pettingall v Pettingall (1842) 11 LJ Ch 176) under which the trustee or executor of the will undertakes to carry out the purpose, and the court grants leave to those persons who would receive the funds if the gift had been declared invalid to approach the court if the trustee or executor fails to carry out the purpose or misuses the funds. The Pettingall order is a judicial attempt to deal with the fact that these are ‘trusts of imperfect obligation’, which are so called because there are no beneficiaries and therefore no persons to whom any genuine obligations are owed to carry out the trust.

Self-assessment questions

1. What anomalous purpose trusts are allowed by law?
2. How does the court provide for their enforcement?
3. What is testamentary delegation?
4. What is the beneficiary principle?
5. Who, if anyone, has a duty to enforce a private purposes trust?
6. What is nonfeasance?
7. What is a true Re Sanderson-type trust?
11.5 Departures from the beneficiary principle

11.5.1 Re Denley’s Trust Deed (1969)

In *Re Denley*, Goff J upheld a trust under which title to land was held on trust for the purpose of providing a recreation ground for the employees of a particular company. Goff J regarded the employees as persons so directly benefited by the purpose that (1) the purpose was not of such an abstract kind as to fall foul of the beneficiary principle, and (2) that the employees had standing to enforce the purpose against the trustees.

Subsequent commentary has tended to treat the case as merely one of a particular kind of discretionary trust (*Re Grant’s Will Trusts* [1980] 1 WLR 360) or as a trust for persons, with the purpose being treated merely as a superadded direction or motive for the gift (*Re Lipinski’s Will Trusts* [1976] Ch 235). In other words, the case appears to have been read so as to deny that it represents a departure from the beneficiary principle.

In any case, the class of beneficiaries must, it is assumed, comply with the certainty requirements laid down in *McPhail v Doulton* [1970] UKHL 1, [1971] AC 424. *R v District Auditor ex p West Yorkshire MCC* [1986] RVR 24, noted by Harpum [1986] CLJ 391, is of relevance on this point. There, a trust for purposes benefiting the residents of West Yorkshire was invalid both because the class of ‘indirect’ beneficiaries was not sufficiently ascertainable, and more simply, it was a private purpose trust.

**ACTIVITY 11.5**

Consider whether it is really necessary for all non-charitable trusts to have a beneficiary and, if so, why?

Is the relevant objection adequately met by the presence of persons benefiting from the carrying out of the purpose as in *Re Denley*?

Should the law in this area be reformed?

**ESSENTIAL READING**

At least one of the following:


**FURTHER READING**


**SAMPLE EXAMINATION QUESTIONS**

**Question 1** ‘No principle has perhaps greater sanction of authority behind it than the general proposition that a trust by English law, not being a charitable trust, in order to be effective, must have ascertained beneficiaries’ (per Lord Evershed MR in *Re Endacott* (1960)).

How accurately does this statement represent the present law relating to the dedication of property to private purposes?

**Question 2** The following provisions are found in Samantha’s will:

a. ‘£20,000 on trust to care for my two favourite horses, Stan and Oliver, for the rest of their lives but for no longer than a period of 21 years’
b. ‘£100,000 on trust to provide a stain-glassed window in my honour in my parish church of St. Cuthberts, depicting me as Mary Magdelene’

c. ‘£50,000 for the organisation and funding of an annual fête at Oak Farm school for 20 years following my death’ (assume this is not a charitable purpose).

Advise Samantha’s executor.

ADVICE ON ANSWERING THE QUESTIONS

Question 1  This is a general survey question of this area of law, focusing on the correct interpretation of the beneficiary principle. A good answer will consider whether a beneficial interest under a trust is required to enforce a trust, or whether an ‘enforcer’ of some kind is sufficient. The view of judges in the leading cases, *Re Astor*, *Re Leahy* and *Re Endacott*, should be discussed. *Re Denley*, as a possible departure from the principle, and its interpretation in subsequent cases, should receive attention, and the existence of anomalous testamentary purpose trusts should be briefly mentioned, along with the oft-expressed judicial view that the categories of valid testamentary purpose trusts are not to be expanded.

Question 2

a. This is valid as an anomalous private purpose trusts (*Re Dean*) properly limited to a valid perpetuity period.

b. This is very similar to the facts in *Re Endacott* and is therefore almost certainly invalid as was the trust in that case.

c. The facts here are similar but not identical to those in *Re Denley*; although no specific class of factual beneficiaries is named, the students of the school might be interpreted to be an appropriate and ascertainable class. On this reading, *Re Denley* and subsequent cases need to be discussed. However, notice that the word ‘trust’ is not employed in this provision; it may merely give a power to spend the money in this way, in which case the power would be valid (*Re Shaw*).

Regarding both (b) and (c), you might briefly advise the executor that the current limitations upon purpose trust remain to an extent controversial, and if the views of a commentator such as Hayton were to persuade a court, an action seeking a declaration that either or both were valid might be appropriate.
**Reflect and review**

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>READY TO MOVE ON</th>
<th>NEED TO REVISE FIRST</th>
<th>NEED TO STUDY AGAIN</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can state the main objections to private purpose trusts.</td>
<td>☐</td>
<td>☒</td>
</tr>
<tr>
<td>I can discuss the interrelationship between the requirement of certainty of objects and the beneficiary principle, and how the beneficiary principle can be seen as a ‘rights’ principle and/or an ‘enforcement’ principle.</td>
<td>☒</td>
<td>☑</td>
</tr>
<tr>
<td>I can discuss cases in which apparent trusts for purposes were held valid and why this does not upset the beneficiary principle.</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>I can describe the few private purpose trusts that will nevertheless be upheld and how they are enforced.</td>
<td>☐</td>
<td>☒</td>
</tr>
<tr>
<td>I can explain why the trust validated in <em>Re Denley</em> is a problematic example of a private purpose trust.</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>11.1 Objections to private purpose trusts</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>11.2 The beneficiary principle and the ‘no purpose trust’ rule</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>11.3 Trusts for persons limited by a purpose</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>11.4 Anomalous valid private purpose trusts</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>11.5 Departures from the beneficiary principle</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>
12 Resulting trusts

Contents

Introduction ......................................................... 130
12.1 When do resulting trusts arise? .................... 131
12.2 Why do resulting trusts arise? ..................... 135
Reflect and review ............................................. 140
Introduction

This chapter is concerned with resulting trusts. You were introduced to them in Chapter 3, where a brief overview of the different types of trust was given. Broadly speaking, a resulting trust is one in which the rights are held by a transferee on trust for the person who made or caused the initial transfer. The word ‘resulting’ comes from the Latin resalire, meaning ‘to jump back’. It should, however, be noted that nothing literally ‘jumps back’. The rights which A previously had are now vested in B, and the rights A has as the beneficiary of a trust are rights A did not have prior to the transfer. It is essential to bear this point in mind in any discussion of resulting trusts, especially the so-called ‘automatic’ resulting trust.

It is also vital to any understanding of resulting trusts to appreciate how they overlap with the other categories of trust. We also touched upon this point in Chapter 3. A trust might be resulting because of proof by evidence that A conveyed the rights to B, declaring that they be held on trust for A. Such a trust would be traditionally called express, not resulting, even though the trust arises in favour of the transferor. So too with money mistakenly paid by A to B. If B holds the mistaken payment on trust for A, as was the case in Chase Manhattan v Israel-British Bank, that could be viewed as resulting (because it arises in favour of the transferor) and constructive (in that it arises for a reason other than a declaration of trust).

The great controversy in this subject is why resulting trusts arise, a controversy not helped by the overlap just mentioned. Some say it is because the law reacts to the presumed (as opposed to proven) intention of the transferor. Others say it is because the law responds to either proof or presumption that the transferor did not intend to benefit the transferee. Others still say that there is no unitary explanation, and that there are in fact at least two distinct reasons why resulting trusts arise. Before examining these theories, we need to ask when resulting trusts arise, for only then can we start to ask why.

ESSENTIAL READING

- Penner, Chapter 5: ‘Resulting trusts’.

LEARNING OUTCOMES

By the end of this chapter and the relevant reading you should be able to:

- state the circumstances in which resulting trusts arise
- outline the competing theories of resulting trusts
- judge which theory best fits the incidence of resulting trusts.
12.1 When do resulting trusts arise?

12.1.1 Express, constructive, implied, and resulting trusts

We have already seen how resulting trusts do not fit into a logical series with express, implied, and constructive trusts, for the word resulting tells us only who is the object of the trust and not, as do the labels express, constructive and implied, why the trust arises. Because they answer different questions, overlaps, as we have seen, are inevitable. In order to avoid such overlaps, the courts have pragmatically limited resulting trusts to three main situations.

Incidence of resulting trusts

There are broadly three situations in which resulting trusts arise:

- the ‘voluntary conveyance’ resulting trust
- the ‘purchase money’ resulting trust
- the ‘failed trust’ resulting trust.

1. The voluntary conveyance resulting trust

If A makes an *inter vivos*, gratuitous transfer of rights to B, and there is no evidence to prove why the transfer was made, a presumption of resulting trust arises. Unless that presumption is rebutted, B will hold those rights on resulting trust for A. The presumption does not apply to testamentary transfers, for it is clear that the testator intends to give their estate away. There are three situations in which the presumption of resulting trust does not apply to transfers *inter vivos* from A to B:

- If A is B’s father or husband, or standing *in loco parentis* (in the place of a father) to B, then a ‘presumption of advancement’ applies instead and B will keep the rights as a gift unless A can rebut that presumption.
- If the right transferred is an interest in the family home of A and B, then it is presumed that ‘equity follows the law’: *Stack v Dowden* [2007] UKHL 17, [2007] 2 AC 432; *Jones v Kernott* [2011] UKSC 53, [2011] 3 WLR 1121. Normally, a resulting trust will not arise, but a ‘common intention constructive trust’ is possible.
- If the right in question is an interest in land, then s.60(3) of the LPA 1925 probably precludes the presumption of resulting trust.

It was accepted *obiter* by the Court of Appeal in *Lohia v Lohia* [2001] EWCA Civ 1691 and *Ali v Khan* [2002] EWCA Civ 974 that the presumption of resulting trust was abolished in the case of a gratuitous transfer of land by s.60(3) of the LPA 1925, which states:

In a voluntary conveyance a resulting trust for the grantor shall not be implied merely by reason that the property is not expressed to be conveyed for the use or benefit of the grantee.

The presumption of resulting trust had its origins in the resulting use. In the early 16th century, a transfer of land for no consideration would give rise to a resulting use for the transferor. The statute of uses 1535 eliminated most uses by ‘executing the use’ and causing legal title to be transferred to the beneficiary of the use. It would execute a resulting use, thereby returning legal title to the transferor and nullifying the transaction, unless the land was transferred ‘unto and to the use of’ the transferee. The statute of uses 1535 was repealed by the LPA 1925 and there is an argument that s.60(3) was included merely as a word-saving provision, without any substantive effect on the modern presumption of resulting trust (compare the treatment of s.56 of the LPA 1925 in *Beswick v Beswick* [1968] AC 58 and s.79 of the LPA 1925 in *Rhone v Stephens* [1994] 2 AC 310).

2. The purchase money resulting trust

A presumption of resulting trust also arises if A *inter vivos* pays C to transfer rights to B, unless the presumption of advancement applies, the rights are the family home

---

1 Word-saving provision: a statutory provision which is intended to reduce the length of written instruments.
of A and B, or the presumption is rebutted by evidence. This is no different from the ‘voluntary conveyance’ resulting trust, discussed above, except that s.60(3) of the LPA 1925 is not relevant. This is not surprising since transfers and purchases are simply two different ways to make gifts. If, for example, you wanted to buy a book from an online bookseller to give to your friend, you could have it delivered either directly to your friend or to yourself to then give to your friend. The transaction is essentially the same in both cases: your friend will receive a book at your expense.

Apart from the effect of s.60(3), should it make any difference whether an apparent gift is made by transfer or purchase? In Dummer v Pitcher (1833) 2 My & K 262, 39 ER 944, a husband transferred some of his stock to himself and his wife as joint tenants. He later purchased more of the same stock for both of them as joint tenants. The presumption of advancement applied to both the transfer and the purchase, but Lord Brougham LC said (at 273) that ‘the presumption of intention to give is considerably stronger’ for the transfer.

A purchase money resulting trust can also arise where A and B inter vivos pay C to convey rights to B. In such a case, B will hold the rights on trust for A and B as tenants in common in shares proportionate to their contribution. For example, in The Venture [1908] P 218 (CA), two brothers contributed funds towards the purchase of a ship. Title was conveyed to one brother alone, and after he died, his widow claimed to be entitled to the ship outright as the beneficiary of his will. She alleged that her brother-in-law had merely loaned his brother the contribution to the purchase price. The contributing brother alleged that he had put the money up on the basis of a partnership. Neither party, however, adduced any evidence in support of their respective allegations. The Court of Appeal held that on proof by evidence of the contribution to the purchase price, a presumption of resulting trust arose in favour of the contributing brother. It was then for the widow to adduce evidence to the contrary, which she had not done. The widow was therefore a trustee for herself and the contributing brother in shares proportionate to the contributions of the two brothers.

3. The failed trust resulting trust

A resulting trust can arise when an express trust fails to dispose of all of its subject matter. This failure can happen either because the trust fails to be valid completely or partially (e.g. for lack of certainty of objects) or because the express trust is fully performed but fails to exhaust the subject matter (e.g. an express trust for B for life with no provision for the remainder). If the failed express trust was self-declared (i.e. with the settlor acting as trustee), nothing further happens: the settlor/trustee merely retains title to the subject matter free of the trust. If the settlor transferred the subject matter to different trustees to hold on an express trust which fails, then normally they will hold the subject matter on resulting trust for the settlor.

Thus, in Morice v Bishop of Durham (1804) 9 Ves 399, 32 ER 656; affirmed [1805] EWHC Ch J80, 10 Ves 522, 32 ER 947 (discussed in the previous chapter), a testatrix left her residuary estate to the Bishop ‘on trust for such objects of benevolence and liberality as the bishop in his absolute discretion might choose’. The trust failed for want of objects and the court held that ‘the property that is the subject of the trust is undisposed of, and the benefit of such trust must result to whom the law gives the ownership in default of disposition by the former owner’.

It is important to note that this type of resulting trust is not based on a presumption. The transfer on trust normally provides sufficient evidence that the trustees were not intended to take the subject matter of the failed express trust for their own benefit. So, there is no need for the presumption of resulting trust and no room for the presumption of advancement. It arises equally in cases of testamentary or inter vivos transfers for the purpose of creating express trusts.

It should not be assumed that a resulting trust is the ‘automatic’ consequence of every failure of an express trust. A resulting trust always arises when the intended express trust is void (e.g. for lack of beneficiaries, as in Vandervell v IRC [1966] UKHL 3, [1967] 2 AC 291, discussed below). Those facts show that the trustee was intended to hold
the subject matter in trust for others and not for their own benefit. However, when the express trust is fully performed leaving a surplus in the trustee’s hands, it may be possible to prove by admissible evidence that the settlor intended the trustee to keep the surplus as a gift. This occurred in several cases in which there had been a close relationship between the settlor and trustee. Their relationship was one of the facts that led the courts to conclude that a gift of the surplus was intended: see *Cook v Hutchinson* (1836) 1 Keen 42, 48 ER 222 (father and son), *Croome v Croome* (1888) 59 LT 582 (CA) (brothers) and *Re Foord* [1922] 2 Ch 519 (brother and sister).

12.1.2 Rebuttal

As we have seen, the first presumption of resulting trust yields to contrary evidence. Thus, if evidence is adduced in the case of a voluntary conveyance which convinces the court that A intended B to take the rights outright (either as a gift or loan), no resulting trust will arise. The presumption which triggers the trust is then said to have been rebutted. Thus, in *Fowkes v Pascoe* (1875) LR 10 Ch App 343 an old lady paid for some shares to be transferred into the names of herself and the son of her daughter-in-law’s second marriage, whom she treated as a grandchild and who lived in her house. The question arose on the lady’s death whether he held the shares for her on trust or whether, as the survivor of joint tenants, they were his absolutely. At first instance, Sir George Jessel MR applied the presumption and held that there was a trust for the old lady’s estate. The Court of Appeal reversed his decision. James LJ asked whether it was possible to reconcile with mental sanity the theory that she put money into the names of herself and the surrogate grandson as trustee upon trust for herself. What object could there conceivably be in doing this? Mellish LJ said that the circumstances showed that it was utterly impossible to come to any other conclusion than that this was intended as a gift, a species of outright transfer.

Another case in the same vein is *Goodman v Gallant* [1985] EWCA Civ 15, [1986] 1 All ER 311 (which was a case concerning the family home, but before *Stack v Dowden*, when the presumption of resulting trust could still apply). A man and a woman contributed unequally to the purchase of a title to land, the woman contributing 75 per cent, the man only 25 per cent. The title was conveyed to them as ‘joint tenants at law and equity’. When they later split up, the woman claimed to be entitled to the benefit of a purchase money resulting trust interest of 75 per cent. The Court of Appeal held that there could be no room for the operation of a presumption when the conveyance contained a declaration of trust.

More recently, in *Westdeutschse Landesbank Girozentrale v Islington LBC* [1996] UKHL 12, [1996] AC 699, a bank paid £2.5 million to a local authority under an *ultra vires* loan contract. The invalidity of the contract meant that the courts treated the payment as gratuitous. The bank argued for a resulting trust, but the House of Lords held that any presumption of trust in favour of the bank was rebutted by proof by evidence that the money was paid under a supposed obligation to make the local authority outright owner. This showed that the bank intended (albeit mistakenly) the local authority to take outright, rather than as trustee for the bank.

**Activity 12.1**

Read *McGrath v Wallis* [1995] 3 FCR 661, and explain the decision.

**The presumption of advancement**

We have seen that the presumption of resulting trust does not arise when B receives an apparent gift (by transfer or purchase) from B’s husband or father or from someone standing in loco parentis to B, in which case a presumption of advancement applies instead. The presumption of advancement was so called because fathers used to be under a moral duty to advance their children in life, and when a child received rights gratuitously from their father, it was assumed that the father had acted to fulfil his moral duty. It is still called the presumption of advancement even though that moral duty no longer applies to fathers (and never applied between husbands and wives).
The presumption is set to be abolished by s.199(1) of the Equality Act 2010:

The presumption of advancement (by which, for example, a husband is presumed to be making a gift to his wife if he transfers property to her, or purchases property in her name) is abolished.

That section has not yet been proclaimed in force. You should ask whether the only effect of this provision, if and when it comes into force, will be to widen the situations in which a presumption of resulting trust will be made. Read the analysis by J. Glister in ‘Section 199 of the Equality Act 2010’ (2010) 73 MLR 807. It is noteworthy that the presumption of advancement now applies equally to fathers and mothers in Australia: Nelson v Nelson [1995] HCA 25, 184 CLR 538. In Canada, mothers and fathers are treated equally, but the presumption of advancement applies only in favour of infant children. Apparent gifts to adult children attract the presumption of resulting trust: Pecore v Pecore 2007 SCC 17, [2007] 1 SCR 795, 279 DLR (4th) 513. Like the presumption of the resulting trust, the presumption of advancement can also be rebutted, though now by evidence showing that the transferor did not intend the transfer to be outright. An example is Warren v Gurney [1944] 2 All ER 472 (CA), where though a father paid for a title to land to be conveyed to his daughter, he retained the title deeds in his possession. On his death, the question arose whether the daughter held her title absolutely or on trust for her father’s estate. The fact that this was a purchase by a father in the name of his daughter raised a presumption of advancement. The Court of Appeal, however, held that the father’s retention of the title deeds showed that he did not intend the daughter to take the title outright, in which case the presumption of advancement was rebutted and a resulting trust arose.

A presumption is an inference that a fact exists. Upon proof by evidence of the existence of relevant facts (e.g. that A transferred company shares to B gratuitously and is not B’s father or husband), the court assumes that an additional fact exists that will have legal significance. There is an ongoing debate about what is being presumed when the presumptions of resulting trust or advancement apply. William Swadling has argued that the presumption of advancement is not a true presumption, but simply a situation in which the presumption of resulting trust does not apply: ‘Explaining resulting trusts’ (2008) 124 LQR 72. He regards the presumption of resulting trust as a presumption that the transferor or purchaser declared a trust for himself. In contrast, Robert Chambers has argued that the presumption of advancement is a true presumption that the transferor or purchaser intended to make a gift: ‘Is there a presumption of resulting trust?’ in Mitchell, C. (ed.), 2010, p.267. He said that the presumption of resulting trust is not a true presumption, but simply a situation in which the presumption of advancement does not apply, in which case, a resulting trust arises because there is no explanation for the transaction.

When one recalls that what is needed to rebut the presumption of resulting trust is evidence that the transferor intended the transferee to take the rights outright and not as trustee, it becomes obvious that the failed trust resulting trust is not normally capable of rebuttal. The reason is that the settlor’s declaration of express trust provides evidence that the settlor did not intend the trustees to take absolutely for their own benefit. Another way of putting this is to say that there is nothing ambiguous about the transfer in such a case. No facts are missing, and so there is nothing to presume. The leading case on this type of resulting trust is Vandervell v IRC [1966] UKHL 3, [1967] 2 AC 291. The facts are complex, but essentially mirror Morice v Bishop of Durham (1804) in that there was a transfer of rights ‘on trust’, but with no beneficiaries identified as objects of that trust. Vandervell, the effective grantor of the right concerned (an option to purchase) argued that there could be no resulting trust in his favour because he had shown that for tax purposes he did not want to be the beneficiary of a trust of that right. However, Lord Wilberforce held that this was irrelevant, for the resulting trust here was not triggered by the operation of a presumption:

The transaction has been investigated on the evidence of the settlor and his agent and the facts have been found. There is no need, or room, as I see it, to invoke a presumption. The conclusion, on the facts as found, is simply that the option was vested in the trustee company as a trustee on trusts, not defined at the time, possibly to be defined later.
It is noteworthy that both Lord Reid and Lord Donovan dissented over the issue of what Mr Vandervell actually intended. They both believed that he had intended to grant the rights outright and not on trust.

Because the presumptions of resulting trust and advancement have no role to play in the ‘failed trust’ cases, Megarry J, in the subsequent case of Re Vandervell’s Trusts (No 2) [1974] Ch 269, christened this type of resulting trust ‘automatic’, which in truth is nothing more than saying that it arose for a reason other than a declaration of trust. In this context, ‘automatic’ is a simply a synonym for ‘constructive’. It does not mean that a resulting trust always arises in this situation. As discussed above, if an express trust is fully performed leaving a surplus, the trustee may be entitled to keep the surplus as a gift if the admissible evidence establishes that is what the settlor intended.

**SELF-ASSESSMENT QUESTIONS**

1. Define ‘resulting trust’.

2. What is the ‘presumption of advancement’?

3. When does a presumption become necessary?

**Summary**

There are three types of resulting trust:

1. The ‘voluntary conveyance’ resulting trust
2. The ‘purchase money’ resulting trust
3. The ‘failed trust’ resulting trust.

The presumption of resulting trust can arise when A gratuitously transfers rights to B or pays for rights to be transferred to B, and there is no evidence to prove what A intended. If A is B’s father or husband or stands in loco parentis to B, then the presumption of advancement applies instead of the presumption of resulting trust. Either presumption can be rebutted by admissible evidence showing what A intended. There is an ongoing debate about what is being presumed.

The presumptions do not apply to the ‘failed trust’ cases, since the circumstances of the transfer to the trustees to hold in trust provide evidence of the settlor’s intention. Exceptionally, in cases where the express trust was fully performed and the settlor and trustee were in a close relationship, the trustee may be permitted to keep the surplus as a gift if it can be proved that this was what the settlor intended.

**12.2 Why do resulting trusts arise?**

Now that we know when they arise, we can begin to address the most contentious issue in resulting trusts: why do they arise? There are several views, which we will now outline. Each is supported by eminent judges and academics and the question is still unresolved. It may help you to take a position on this question which you can defend in the examination. You will not be penalised for adopting one with which the Examiners may disagree.

The essential questions to consider are (a) what are the facts (established either by evidence or presumption) that will give rise to a resulting trust in each of the three different traditional categories, and (b) are these facts the same or different in each of those categories?

According to Lord Browne-Wilkinson in Westdeutsche, all resulting trusts arise because of a presumption that the transferor intended to create a trust for himself. So far as the first type of resulting trust is concerned, his lordship’s view makes some sense if there is a gap in the evidence and therefore some room for a presumption to operate. It does, however, require one qualification. As we have seen, a mere intention to create a trust normally has no effect. The intention must be manifested, or expressed. Since presumptions are merely creatures of the law of procedure, facts proved by
presumption can logically have no greater force than facts proved by evidence. As a consequence, Lord Browne-Wilkinson might have spoken of a presumption of 'manifested intention' or presumption of 'declaration of trust', so making the 'presumed resulting trust' a species of express trust. Exactly why the law should find a declaration of trust proved by presumption in such circumstances can only be explained by reference to legal history, and in the attempt of holders of titles to land to escape the burdens of feudalism.

Where Lord Browne-Wilkinson’s analysis breaks down, however, is in thinking that a presumption can operate with regard to the ‘failed trust’ resulting trust. However, it cannot explain a case like Vandervell, where it is absolutely clear that Mr Vandervell did not want to create a trust for himself. It also fails to explain numerous cases in the other categories where the evidence is clear that the transferor or purchaser did not make a declaration of trust nor intended to create a trust. For example, in Brown v Brown (1993) 31 NSWLR 582 (CA), a mother’s house was sold and the proceeds used to purchase a house for her sons. The presumption of advancement applied (to mothers in Australia), but was rebutted because she never thought about the consequences of the transaction and therefore never formed the intention to make a gift. She never formed an intention to create a trust for herself and certainly never declared a trust, but the resulting trust responded to evidence that no gift was intended.

According to Lord Millett, all resulting trusts respond to the absence of intention to benefit the recipient. He has expressed this view writing extra-judicially in ‘Restitution and constructive trusts’ (1998) 114 LQR 399. It also provided the basis for the Privy Council’s advice in Air Jamaica Ltd v Charlton [1999] UKPC 20, [1999] 1 WLR 1399. In that case, a pension fund trust failed because it violated the common law rule against perpetuities. Clause 4 of the trust deed stated: ‘No moneys which at any time have been contributed by the Company under the terms hereof shall in any circumstances be repayable to the Company.’ It was argued that this prevented a resulting trust in favour of the company, but this was rejected by the Privy Council. Lord Millett said (at [45]):

In Re ABC Television Ltd Pension Scheme, unreported, 22nd May 1973, Foster J. held that a clause similar to clause 4 of the present Trust Deed ‘negatives the possibility of implying a resulting trust’. This is wrong in principle. Like a constructive trust, a resulting trust arises by operation of law, though unlike a constructive trust it gives effect to intention. But it arises whether or not the transferor intended to retain a beneficial interest – he almost always does not - since it responds to the absence of any intention on his part to pass a beneficial interest to the recipient. It may arise even where the transferor positively wished to part with the beneficial interest, as in Vandervell v Inland Revenue Commissioners [1967] 2 AC 291.

According to Swadling, the fact proved by presumption is a declaration of trust: ‘Explaining resulting trusts’ (2008) 124 LQR 72. This can be supported both by legal history and logic in the case of the ‘voluntary conveyance’ and ‘purchase money’ resulting trusts. As with Lord Browne-Wilkinson’s view, the difficulty it encounters is trying to explain the numerous cases in which resulting trusts have arisen even though it was clear that the transferor or purchaser never declared a trust. Swadling does not address the ‘failed trust’ cases.

According to Chambers, the presumptions are no longer important except in cases where relevant evidence is inadmissible because it would reveal an illegal purpose (Mitchell, C. (ed), 2010, p.267). In almost every case, there is sufficient circumstantial evidence to allow a court to decide what the parties intended. For example, in Lohia v Lohia [2001] EWCA Civ 1691, land was transferred from a father and son into the father’s name alone. Many years later, after the father was dead, the son claimed that the land was held on resulting trust for the father’s estate and the son in equal shares, and testified that the transfer was a forgery. The trial judge rejected the son’s evidence of forgery and decided that the transfer must have been part of some family arrangement in which the father was intended to receive title for his own benefit. In other words, very slender circumstantial evidence was sufficient to rebut the presumption of resulting trust (and it was unnecessary to decide whether the
presumption was displaced by s.60(3) of the LPA 1925). The outcome would have been the same regardless of which presumption (if any) applied at the start.

The real worry are the cases involving illegal purposes: if evidence of intention is wholly inadmissible, the presumptions can lead to arbitrary (and therefore unjust) outcomes. In Tinsley v Milligan [1993] UKHL 3, [1994] 1 AC 340, a same-sex couple purchased a home together in Tinsley’s name. They then pretended to the Department of Social Services that Milligan was only a lodger and fraudulently obtained housing benefits to pay her rent. The House of Lords held that evidence of Milligan’s contribution to the purchase price gave rise to a presumption of resulting trust in her favour which could not be rebutted because evidence of their intention was inadmissible due to illegality. This was the just result in the particular case, since this is what the parties intended, both were complicit in the fraud, and there is no reason why one fraudster should obtain a windfall at the other’s expense. However, the result would have been different if the presumption of advancement had applied (if Milligan had been Tinsley’s husband or father). There is no reason why this additional fact, which has nothing to do with the illegality at the heart of the case, should reverse the outcome. If the presumption of advancement is ever abolished by s.199 of the Equality Act 2010, it will help reduce the potential for arbitrariness.

As discussed above, it was decided in Stack v Dowden that the presumption of resulting trust no longer applies to the family home. So if Tinsley v Milligan had been decided after that case, the outcome should have been different. However, in O’Kelly v Davies [2014] EWCA Civ 1606, an unmarried couple purchased a house as joint tenants as their family home and later transferred it into the woman’s name alone so that she could make a false claim for social security benefits and child support by pretending to be a single mother living alone with her child. Following Jones v Kernott, the Court of Appeal decided that she held the home under a common intention constructive trust for both parties, and not under a resulting trust. It also decided that the parties could establish their common intention without relying on their illegal purpose. It is not clear why this same approach did not apply in those cases in which a father or husband could not rebut the presumption of advancement because of his illegal purpose. Could he now say that he did not intend to make a gift, but intended to create a trust, without relying on the illegal purpose for creating that trust?

Chambers believes that all resulting trusts arise for the same reason, because the recipient has obtained assets that were not intended to be retained for their own benefit. In most cases, this is established by evidence, but presumptions of resulting trust or advancement may have a role to play in some cases. In many cases, the transferor or purchaser will intend to create a trust for themselves, and if expressed in the proper form, this should give rise to an express trust. However, evidence of an absence of intention to give is sufficient to give rise to a resulting trust: Hodgson v Marks [1971] EWCA Civ 8, [1971] Ch 892; Vandervell v IRC [1966] UKHL 3, [1967] 2 AC 291; Air Jamaica Ltd v Charlton [1999] UKPC 20, [1999] 1 WLR 1399. This is similar to Lord Millett’s view. Where they differ is that Chambers believes that resulting trusts should have a wider role and apply in cases of mistake (like Chase Manhattan Bank NA v Israel-British Bank (London) Ltd [1981] Ch 105). Lord Millett believes that resulting trusts should be limited to cases where there was a complete absence of intention to benefit the recipient. A mistaken intention to confer a benefit is in his view sufficient to preclude a resulting trust.

Activities 12.2–12.4

12.2 Read The Venture (1908). What does this case tell you about the presumption which triggers some resulting trusts?

12.3 Read Vandervell v IRC (1966). What is the difference between the approach of the Court of Appeal and the House of Lords to the resulting trust of the option to purchase?

12.4 How might Lord Browne-Wilkinson argue that the failed trust resulting trust can be explained as arising to reflect the presumed intention of the transferor? How might Lord Millett respond to that argument?
**Essential Reading**

At least one of the following

- Martin, Chapter 10: ‘Resulting trusts’.
- Oakley, Chapter 9: ‘Implied or resulting trusts’.
- Pettit, Chapter 9: ‘Resulting trusts’.

**Further Reading**

- Hayton & Mitchell, Chapter 14: ‘Resulting trusts’.

**Sample Examination Questions**

**Question 1** ‘Both types of resulting trust are traditionally regarded as examples of trusts giving effect to the common intention of the parties. A resulting trust is not imposed by law against the intentions of the trustee (as is a constructive trust) but gives effect to his presumed intention’ (Lord Browne-Wilkinson in Westdeutsche Landesbank Girozentrale v Islington LBC [1996]).

Discuss.
Question 2  A week before he died, Fred conveyed a freehold title to land and some shares to his son, Joe, to be held on trust for ‘such objects of benevolence and liberality as Joe in his absolute discretion might choose’. By his will, Fred left all his real and personal estate to his wife, Sarah.

Advise Sarah.

Advice on answering the questions

Question 1  This essay is directed to the vexed question why resulting trusts arise. A good answer would begin by explaining what resulting trusts are and stating when they arise. It would then outline the views of the major players in the debate, taking careful account of the precise state of the law here, noting especially that some of Lord Browne-Wilkinson’s comments in Westdeutsche were obiter, while those of the House of Lords in Vandervell were ratio. Candidates might also question Lord Browne-Wilkinson’s focus on the intentions of the trustee rather than the settlor. Where evidence is adduced to prove that a declaration of trust has taken place, no enquiry is made into the state of mind of the transferee. This must equally be the case where a resulting trust arises in response to a presumption.

Question 2  In answering this short question, candidates should start by outlining how the problem would be resolved using the orthodox theory of resulting trusts contained in Vandervell v IRC (1967). According to Lord Wilberforce, this would not be an occasion for presuming that Fred intended Joe to hold the rights on trust for Fred, because Fred made it clear that he wanted them to be held on other trusts, although those trusts were void. The failure of the intended trusts would mean, as per Lord Upjohn and Lord Wilberforce, that Fred never divested himself of his beneficial interest, with the consequence that Joe will now hold the rights on a resulting trust for Fred arising by operation of law. Using Lord Millett’s approach, Joe would also be a resulting trustee for Fred, since proof by evidence that Joe was meant to be a trustee also proved that Joe was not meant to take beneficially.

It is slightly more difficult to analyse this case according to Lord Browne-Wilkinson’s views. According to him, the situation is governed by presumptions of intent. Normally, he would say that, in the circumstances, a presumption operates to the effect that Fred wants the rights back, so a presumed resulting trust will arise in his favour. However, since we are dealing with presumed intentions, we should apply the presumption of advancement to transfers between father and son, which means that Joe will take at least the shares absolutely unless further evidence is adduced to rebut that presumption. The declaration of (the failed) express trust would provide sufficient evidence that no gift was intended and rebut that presumption. The transfer of land is simpler, for there the presumption of resulting trust has supposedly been abolished in the case of gratuitous conveyances of land (which this is), with the result that we anyway start, at least we assume we start, from a presumption of advancement.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>I can state the circumstances in which resulting trusts arise.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can outline the competing theories of resulting trusts.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can judge which theory best fits the incidence of resulting trusts.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked 'need to revise first', which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>12.1 When do resulting trusts arise?</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>12.2 Why do resulting trusts arise?</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
13 Rights ‘held’ by unincorporated associations

Contents

Introduction .................................................. 142
13.1 Gifts and other transfers to unincorporated associations ............... 143
13.2 The distribution of rights upon dissolution ......................... 145
Reflect and review ........................................... 150
Introduction

An unincorporated association is a group of individuals who combine to act together to achieve some purpose, often social. Examples are bridge clubs and student law societies. How do such associations hold rights? How, for example, does a student law society hold the funds which it acquires through the collection of dues, or the profits from the events it organises? As the society is not incorporated, it has no legal personality in itself and so cannot hold rights in the way that a company can. These are the questions this chapter addresses. The material covered in this chapter is somewhat marginal to the law of trusts. Once properly understood, the problem of how rights are held by unincorporated associations can be seen typically to employ trusts in a quite straightforward fashion, and at first glance this rather simple use of the trust does not deserve a chapter in its own right. But the importance of the material in this chapter lies in the somewhat tortured history of the case law, by which several mistaken approaches to the question created a series of misunderstandings about trusts.

Clarifying these, so that such mistakes do not cloud your understanding of the law of trusts, is the primary purpose of looking at this material in some detail. Two topics in particular must be addressed:

- the proper construction of gifts and other transfers to an unincorporated association, and
- the destination of such rights when the association dissolves.

Although the two are inextricably linked, it is not unusual to find them dealt with separately in the standard textbooks.

The work in this chapter builds on that already studied in Chapter 11: ‘Purpose trusts II: private purposes’, and Chapter 12: ‘Resulting trusts’, and you should reacquaint yourself with those chapters now.

Essential reading

- Re-read Chapter 11: ‘Purpose trusts II: private purposes’.
- Re-read Chapter 12: ‘Resulting trusts’.

Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- explain why gifts and other transfers to unincorporated associations give rise to problems of construction for the courts
- describe the different constructions a court might place on such a gift or other transfer
- explain the contract-holding theory of right-holding and why holding rights that way does not offend the rule against private purpose trusts
- explain what happens to rights given to an unincorporated association when the association is dissolved.
13.1 Gifts and other transfers to unincorporated associations

Although the unincorporated association itself is not a legal person, and so has no capacity to hold rights, people nevertheless insist on trying to transfer rights to it, either by way of gift or pursuant to some contract which they believe they have with the association. It is then for the courts to try to make sense of what is, as a matter of law, a nonsensical act. Although courts could just say that such a transfer was void, as they would, for example, say of a transfer to a tree or to my pet cat, they try to find a way to validate the transfer. Their method is to say that even though the association itself has no legal personality, its members and officers do. The transfer is therefore to be construed as one to the members or officers of the association. The question then is the capacity in which those members or officers hold the rights received.

13.1.1 A transfer to members in equal shares

Traditionally, the courts took the simplest approach, and viewed such transfers as made to all the members personally (either directly as co-owners of the rights, usually money, or through the medium of a trust, the treasurer or other officers of the club acting as trustee). This interpretation would allow each member of the association to claim their share of the right, and use the money as they wished, and this would, obviously, normally be against the intentions of the donor.

13.1.2 A purpose trust

Probably in view of the last consideration, courts occasionally regarded the transfer as made to the members or officers of the association on trust, not for the members themselves but for the purposes of the association. This would prevent individuals from claiming and taking away their individual shares, for they would not be beneficiaries under a purpose trust. But this approach is disastrous for the transferor, because it would generally invalidate the transfer as a private purpose trust, unless the purposes were exclusively charitable (see Leahy v A-G for New South Wales [1959] UKPC 1, [1959] AC 457).

13.1.3 Contract-holding theories

A third, more recent, approach is to resort to contractual notions rather than the device of the trust. It takes advantage of the fact that unincorporated associations always proceed on the basis of explicit or implicit understandings between the members, which give rise to duties between them. As these understandings and obligations are mutual and consensual, in law they are contractual relations, even if informal. Of course, some clubs are very formal about their understandings. They produce constitutions and rules and organise themselves into committees and so on. But even the most informal association operates by contractual obligations, however informal they are, if it is an association at all. Recognising the existence of these contractual obligations expressed in the club rules, where possible, gifts and other transfers to such associations are construed as being transfers to the members themselves, but subject to their contractual obligations *inter se* (‘between themselves’) to use the rights so given to promote the purposes of the association: Re Recher’s WT [1972] Ch 526; Re Lipinski’s WT [1976] Ch 235. The reason why this construction works is that it uses a contract to control the expenditure of the fund rather than the terms of a trust, so that the carrying out of the purpose is enforced by way of compliance with a contract, not by way of a trustee’s carrying out a private purpose trust. There are, however, two variants of this ‘contract-holding theory’: the ‘bare trust/contractual mandate’ solution and the ‘purely contractual’ approach.

A bare trust/contractual mandate solution

This solution recognises the contractual aspect of right-holding by unincorporated associations, but also recognises that the contractual obligations of the members between themselves almost always work in combination with a trust, as follows. Recall the discussion of bare trusts in Section 3.2 of this guide. In such cases, the trustees
hold the rights to the order of the beneficiaries. At any one time, however, the trustees may be given orders as to how to deal with the rights. These orders, sometimes called mandates, allow the trustees to deal with the trust rights without acting in breach of trust. Without such a mandate, they would be acting in breach of trust. The way in which unincorporated associations take advantage of this is to control the giving of mandates to the trustees of the association by way of contract. The rights of the association are held on trust by one or two members of the association (usually the treasurer and another officer) for all the members in equal shares. The association’s rules provide the mandates authorising the trustees to use the rights, perhaps directly but more likely by providing the procedures for making decisions, whether by committee, or by unanimous vote, etc. In this way, the rights are held for the purposes to which the members want them put, not under a purpose trust, but as the result of their contract governing the way their own rights, which are held under a bare trust, are dealt with.

A purely contractual approach

This ‘bare trust/contractual mandate’ interpretation of the situation is not the only one that might work, but it is the best. We can compare it to the ‘purely contractual approach’. Under this, the members all individually hold the rights as co-owners, so there is no trust, but they are bound by their contract between themselves to deal with the rights as decided by the association rules, etc. There are two problems with this solution. The first is that co-ownership without a trust is wholly impractical when there are more than three or four members. They cannot all be signatories of the association’s bank account or parties to the lease or licence of its premises. To function properly, one or two members of the association will have to hold rights in trust for the others.

The second problem is making sense of gifts (or other transfers) to the association. A person cannot give rights ‘subject to contract’. You cannot give a friend rights to be held on the terms of a contract with another party, for a contract is a personal obligation between individuals, and you are not privy to their contract. In ‘A problem in the construction of gifts to unincorporated associations’ [1995] Conv 302, Matthews suggested that the members of an association could avoid this problem by incorporating in their rules a provision that any gifts or contractual payments (for example, money received for tickets to a dance the association sponsors) received are taken by members individually but subject to their contract. While this could work, on this basis the members bind themselves by contract to treat transfers to them in a certain way, it is fanciful to think that many associations have such rules.

Rather, the court reasons using the bare trust/contractual mandates approach as follows: when a donor makes a gift to an association, they make it on trust by making an addition to the current trust by which the trustees hold other rights so given. Anyone can settle rights by transferring them to trustees on trust to hold them in the same way as they hold other trust rights. This happens, for example, when employers and employees make regular contributions to a pension fund. The trust upon which the additional funds are held is determined by reference to the already existing trust. This is how such gifts are treated as ‘accretion to the funds’ of the association (Re Recher’s WT), with the court never bothering to enquire as to whether the rules of the fund provide for Matthews’ purely contractual approach.

13.1.4 The construction of transfers to associations and transfers to political parties

To achieve the bare trust/contractual mandate solution, the courts have been prepared to ignore words which in other contexts would suggest that a true purpose trust is intended (e.g. ‘solely’ in Re Lipinski’s WT), although they will not construe a gift as one to the members where the members do not have complete control of the rules of the association: Re Grant’s WT [1980] 1 WLR 360. This case concerned a local Labour Party constituency association, and the court held that it did not fulfil the requirements of an unincorporated association, but the reasoning is doubtful. In Conservative and Unionist Central Office v Burrell [1981] ECWA Civ 2, [1982] 2 All ER 1, [1982]
1 WLR 522, the Court of Appeal held that political parties were ‘political movements’, not unincorporated associations, and so the bare trust/contractual mandate solution could not work, since movements do not have the membership of an association (although it is not clear why political parties cannot be associations with a definite membership even if they are political). Instead, the court explained a gift to the party in Burrell as given under an agency arrangement, with the treasurer to use the funds for the purposes of the party as the donor’s agent. This construction is unsatisfactory in more ways than one, failing in particular to account for testamentary gifts (i.e. gifts made in a will) for when a will comes into operation the testator is dead, and a dead person cannot be a principal for any agent.

**Self-assessment questions**

1. Why does an attempted transfer of rights to an unincorporated association give rise to problems?

2. Why is a transfer to the members as co-owners outright likely to defeat the donor’s purpose?

3. Why are such transfers not construed as transfers on trust for the purposes of the association?

4. What are the contractual obligations of the members? Give some examples.

5. What is a contract-holding theory by members of an unincorporated association?

6. What are the two different versions of the contract holding theory, and which is preferable?

7. How have the courts construed attempted transfers to political parties? What difficulties arise with this construction?

**Essential reading**

At least one of the following:

- Martin, Chapter 14: ‘Non-charitable purpose trusts’, Sections 5 ‘Unincorporated associations’, 6 ‘Mandate or agency’.


**Further reading**


**Activities 13.1 and 13.2**

Read Re Lipinski’s WT [1976] Ch 235 and answer the following questions:

13.1 What was the expressed purpose of the gift? On your reading, would you say that the settlor intended the money to be used solely for a particular purpose?

13.2 On what basis or bases did Oliver J hold the gift valid?

**13.2 The distribution of rights upon dissolution**

The correct assessment of how rights were received and held will also explain what is to happen to any funds that remain when the association dissolves. While that is obviously correct, too often the case law decisions regarding the distribution of rights on dissolution have proceeded on the basis that the association itself held funds in ways that would have been untenable, if that basis had been examined in terms of how gifts or other transfers were validly made to the association.

For example, on dissolution the court might unwittingly proceed on the basis that the funds were given and held on private purpose trusts, which would have made...
those gifts invalid at the outset, given that private purpose trusts are invalid. Indeed, the distinction in the law between the cases dealing with the validity of gifts to unincorporated associations and the law found in cases dealing with the dissolution of associations is such that the two lines of cases are basically irreconcilable. It has not helped matters that these two topics were generally treated separately in texts and treatises. It was only with the recent development (from *Re Recher’s WT*) of the bare trust/contractual mandate theory that a sensible reconciliation has begun. For that reason, cases on the dissolution of unincorporated associations decided earlier must be read with care.

13.2.1 How were the rights originally received?

The key question to ask here is how the rights were received, for that will tell you how they were held to the time of dissolution. The question to then ask is how, if at all, dissolution has changed that entitlement. If the association’s purposes were charitable, and the rights were held by its officers/members on trust for charitable purposes, the rights will be applied *cy-près* to a similar purpose (see *Re Vernon’s WT* and *Re Finger’s WT*, discussed in Section 10.5). In the unlikely event that the rights were held on trust for valid non-charitable purposes (recall that there are some valid non-charitable purposes, discussed in Section 11.4), then the trust should not fail, as the winding up of the association will not in itself be a winding up of the purpose. Unfortunately, most decisions in which the court takes the view that the rights were held on purpose trusts regard the purpose, quite wrongly of course, as the purposes of the association, a purpose which then fails because of the dissolution of the association. On this interpretation, a resulting trust should arise in favour of those who originally contributed the right. Where the rights were received under either version of the contract-holding theory elaborated above, they will simply be distributed among the membership existing at the time of dissolution, because under the contract-holding theories the members of the association hold the rights outright. When the association dissolves, their contractual obligation to use the rights in a particular way simply disappears, so that they can distribute the rights to themselves in equal shares, or do anything else with them they want.

13.2.2 Some wrongly decided cases

*Re Printers and Transferrers Amalgamated Trades Protection Society* [1899] 2 Ch 184 and *Re Hobourn Aero Components Ltd’s Air Raid Distress Fund* [1946] Ch 194 concerned rights collected to provide benefits to members of employees’ associations. In both cases, when the associations dissolved, the court held that there was a resulting trust of the remaining rights in favour of the members in proportion to their contributions. As this was a resulting trust, the court must have regarded the funds as held upon purpose trusts which failed when the associations dissolved. Such private purpose trusts, however, are invalid. On the contract holding theory, the result would be essentially the same – on dissolution, the rights would be distributed to the members, and presumably their individual shares would be determined by the terms of the association, even implicit terms, and shares proportionate to contributions might well have best reflected their mutual understanding.

*Cunnack v Edwards* [1896] 2 Ch 679 (CA) concerned an association which provided benefits to the widows of deceased members, paid from a fund to which the members contributed. Upon dissolution, the court reasoned that the members had received all they had contracted for (i.e. the provision of pensions for widows), so the surplus went to the Crown as *bona vacantia* (ownerless goods). As with the preceding two cases, the only possible basis for this finding was that the rights were devoted to a private purpose trust, to provide pensions for members’ widows, which failed upon dissolution. Yet the application of a kind of ‘contract theory’ to private purpose trusts (that donors donate to the purpose trust thereby contracting with the trustees to obtain a particular personal benefit out of the purpose), makes a nonsense of the idea that the money is held genuinely on purpose trust. This is an anomalous case, and it is difficult to put any reasonable construction on it.
**Reflection Point**
Cases are sometimes wrongly decided. Why do wrong decisions occur? How much reliance can we place on judges’ decisions? How does this relate to the doctrine of precedent?

**13.2.3 Modern dissolution cases**

Re West Sussex Constabulary’s Widows, Children and Benevolent (1930) Fund Trusts [1971] Ch 1 and Re Bucks Constabulary Widows’ and Orphans’ Fund Friendly Society (No 2) [1979] 1 WLR 936, [1979] 1 All ER 623 both addressed the dissolution of associations of members of particular police forces in England. Re West Sussex basically followed the earlier flawed cases, even drawing in part upon Cunnack v Edwards. Re Bucks, by contrast, applied the modern contract-holding theory and held that on dissolution, the rights were held by the members of the association outright.

In Hanchett-Stamford v A-G [2008] EWHC 330 (Ch), [2009] Ch 173, Lewison J carefully reviewed and followed Re Bucks with one important exception. In Re Bucks, Walton J suggested (as obiter dictum) that an association’s assets would become ownerless if the association ceased to exist and therefore become bona vacantia. In Hanchett-Stamford, an association (the Performing and Captive Animal Defence League) had ceased to exist when there was only one member left (since a single person cannot associate or make contracts with himself). She was absolutely entitled to the association’s assets for her own benefit (which she then donated to the Born Free Foundation, a registered charity).

**13.2.4 A restitutionary solution in certain cases**

It has been noted that while the contract-holding theories do provide for a workable legal construction for rights given to unincorporated associations, such a construction does not ensure that donors who donates money to an association for the use of the association in its activities will get what they want, for the association may always change its rules or goals (as a contractual relationship it can always be varied by consent of the parties) and thus devote its funds to other activities. The members might even decide to disband the association and divide its remaining funds among themselves. In light of this, Swadling has proposed that a disgruntled donor could claim that their gift was made on condition that it be used for a specified purpose (Swadling, W.J. ‘Property: general principles’ in Burrows, A. (ed.), 2013). This is not a purpose trust, but a conditional gift recognised at common law. If this construction can be put on the gift, and the gift is not devoted to the purpose, the donor can bring a personal action under the law of unjust enrichment for restitution of an equivalent sum.

**Self-assessment questions**

1. What does it mean to say that an unincorporated association is dissolved?
2. How do the members’ contractual relations change upon dissolution?
3. Under the contract-holding theory, how does the dissolution of an unincorporated association affect the members’ rights in rights given to the association?
4. How is the law concerning conditional gifts relevant to the dissolution of an unincorporated association?

**Essential reading**

At least one of the following:

- Martin, Chapter 10: ‘Resulting trusts’, Section 2 ‘Conveyance to trustees’, Part ii ‘Surplus funds on dissolution of unincorporated associations’.
- Oakley, Chapter 9: ‘Implied or resulting trusts’, Section V ‘Failure of a trust or its beneficial interests’ and Section VI ‘Resulting trusts arising as a result of void or voidable transactions’.
• Pettit, Chapter 9: ‘Resulting trusts’, Section 1 ‘Failure to dispose of the equitable interest’.

• Cases: Re West Sussex Constabulary’s Widows, Children and Benevolent (1930)

FURTHER READING

• Hayton & Mitchell, Chapter 14: ‘Resulting trusts’, Section 3 ‘Failing trusts’ Part C ‘Dissolution of unincorporated associations’.


ACTIVITY 13.3

Read Re West Sussex (1971), Re Bucks (1979) and Hanchett-Stamford (2008).

Explain how these decisions differ in their approach to the way that rights are ‘held’ by unincorporated associations, and which view is better.

SAMPLE EXAMINATION QUESTIONS

Question 1 How are rights purportedly given to unincorporated associations held, and what rules govern the distribution of such rights upon dissolution?

Question 2 In 1989, the 20 members of the Bloomsbury Rock-climbing Club each transferred £2,000 on trust to their trustee-treasurer to hold as the ‘Accident Fund’ pursuant to a resolution of their annual meeting. The minutes of the meeting disclose that the fund was to be invested, and money be paid out to a member or his or her surviving spouse on a certain payment scale should the member be injured or die as a result of a rock-climbing accident. Since that time, further contributions to the fund have been received from new members upon joining, and other funds have been added as a result of various fund-raising events. The payment scale has been updated from time to time, and one payment of £25,000 has been paid to the widower of a member who died climbing, and further amounts totalling £25,000 have been paid to members following non-fatal accidents. By January, 2008, the club’s membership had dwindled to three members, and two of these died in a rock-climbing accident, leaving only the treasurer trustee. Following payments to the surviving spouses, the funds stand at £43,000. Advise the trustee-treasurer as to how he should distribute these funds.

ADVICE ON ANSWERING THE QUESTIONS

Question 1 A good answer will distinguish this situation from that of a purpose trust, and will explain the contract-holding theory and its consequences for the distribution of funds on dissolution. The prior law concerning the construction of gifts to unincorporated associations, in particular that the gift is a gift to members to take as co-owners outright, or is a gift on purpose trust, should be canvassed to show its weaknesses, and the two versions of the contract-holding theory should be explained.

Similarly, with the distribution of rights on dissolution, a good answer would consider the earlier law leading up to Cunnack v Edwards, and then go on to consider the more recent developments in Re West Sussex, Re Bucks and Hanchett-Stamford, explaining why Re Bucks and Hanchett-Stamford express the better view. It would explain how the law concerning construction of gifts and other transfers to unincorporated associations must match up with the law concerning the distribution of rights upon their dissolution.

Question 2 According to the modern law which embraces the contract-holding theory, there is no room for a purpose trust analysis here, though past case-law which seems to indicate this as the best analysis might be considered and shown to be flawed. A purpose trust construction is possible, though it would not seem that the setting up of this fund should be invalidated given the decision in Re Lipinski.
The issue is clearly that, as the sole remaining member of the club, the treasurer-trustee now holds the rights outright on contract-holding principles: *Hanchett-Stamford*. This may appear unjust, though it must be remembered that such a result flows from the law, and it is not clear that any past member has any right to complain, for a contractual provision dealing with the situation might always have been made. Indeed, the first piece of advice to the treasurer-trustee is that the rules of the association, or common understandings as expressed in various minutes, should be examined to see whether any guidance on this situation can be given. If not, it would appear that the funds belong to the treasurer-trustee. The *bona vacantia* result as applied in *Cunnack v Edwards* has little to commend it. Lastly, the restitutionary approach might be considered. If the various contributions can be construed as conditional gifts (which appears most strained in the case of funds raised at events), then the treasurer-trustee might be bound to make restitution of the funds to past contributors on some sort of pro-rata basis.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th></th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can explain why gifts and other transfers to unincorporated associations give rise to problems of construction for the courts.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can describe the different constructions a court might place on such a gift or other transfer.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain the contract-holding theory of right-holding and why holding rights that way does not offend the rule against private purpose trusts.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain what happens to rights given to an unincorporated association when the association is dissolved.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>13.1 Gifts and other transfers to unincorporated associations</td>
<td></td>
<td></td>
</tr>
<tr>
<td>13.2 The distribution of rights upon dissolution</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Contents

Introduction ................................................. 152

14.1 The appointment, retirement and removal of trustees in outline ................................ 153
14.2 Powers in the trust instrument. ................................................. 154
14.3 Powers under ss.36 and 39 of the Trustee Act 1925 ................................................. 154
14.4 Powers under s.19 of the Trusts of Land and Appointment of
Trustees Act 1996 ................................................. 155
14.5 The statutory and inherent jurisdiction of the court ................................................. 156
14.6 The vesting of the trust rights upon a change of trustee(s) ................................................. 157
Reflect and review ................................................. 160
Introduction

The trust is operated by the current trustees since the trustees of a trust may change over the life of the trust. It is essential first that there are trustees to carry out the trust, and second that the current trustees are capable of carrying out the trust and fit to do so.

A trustee may become incapable of carrying out the trust because of illness or mental incapacity or may become unfit to carry out the trust because they are revealed to be dishonest, or because their own interests are in conflict with their duties under the trust. It is therefore essential that there are powers to appoint new trustees, to allow trustees to retire, and to remove trustees. Such powers can be conferred by the settlor when the trust is created, by statute, or may lie within the jurisdiction of the court in its general supervisory role over trusts. Although these powers are simple to understand in principle, their exercise can be somewhat technical and generally involve taking a number of considerations into account. This is especially true in respect of the operation of powers conferred by statute. Different sorts of considerations apply to the appointment, retirement and removal of trustees, and we will examine each in turn.

Essential reading

- Penner, Chapter 10: ‘The trust up and running’, paras 10.48–10.57 (‘Appointment, retirement, and removal of trustees’).

Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- give examples of circumstances in which the appointment, retirement, or removal of a trustee is desirable or necessary
- explain why the statutory powers of appointment, retirement, and removal of trustees are generally relied upon in preference to powers in the trust instrument or the jurisdiction of the court
- explain how the statutory powers found in ss.36 and 39 of the Trustee Act 1925 and s.19 of the Trusts of Land and Appointment of Trustees Act 1996 work, and explain the extent to which they are fiduciary powers
- explain the court’s powers in relation to the appointment and removal of trustees
- explain when, why, and how rights held on trust are dealt with upon a change of trustees.
14.1 The appointment, retirement and removal of trustees in outline

14.1.1 The appointment of first trustees

In the case of an inter vivos trust, the appointment of the first trustees is generally straightforward. In the case of a self-declaration of trust, the settlor is of course himself the first trustee. In the case of a trust constituted by transfer of the subject matter to trustees, such persons become trustees when it is received. Trusts are generally created by using a written document (the trust instrument) which recites the terms of the trusts and is often the instrument that constitutes the trust (e.g. it operates as a deed of transfer of title to chattels). This document will name the first trustees of the trust. Problems are more likely to arise in the case of testamentary trusts (i.e. trusts that come into effect as part of the testator-settlor’s will). In many cases, the first trustees of the trust will be the same persons appointed as the executors of the will. However, a person nominated under a will to be executor or trustee can refuse the appointment or may have died by the time the will comes into operation upon the testator’s death. Thus, powers of appointment held by someone other than the settlor may be needed even to appoint the first trustees.

14.1.2 Appointment of new trustees and the discharge of trustees

There are three basic occasions when it may be necessary to appoint new trustees:

1. upon the death of a human trustee, or more rarely, upon the effective incapacitation of a trust company (due to insolvency or loss of the right to carry on a trust business)
2. on the occasion of the retirement or removal of a trustee
3. where it is desirable to increase the number of trustees.

Generally speaking, it is regarded as essential that a trust be conducted by a minimum of two trustees (as joint owners of the relevant rights) for two main reasons. First, it is felt that the opportunities for fraud or incompetent dealing are much reduced when decisions are taken by two persons rather than one. Second, where the trust assets include interest in land it is essential that the there are two trustees for the trustee to provide a proper receipt for purchase monies if that land is later sold: Trustee Act 1925, s.14; LPA 1925, s.27. Note that these sections provide an exception for a ‘trust corporation’ to act as sole trustee. This is not the same thing as an ordinary trust company, but has a special meaning: Trustee Act 1925, s.68(18); LPA 1925, s.205(1) (xxviii). Also note that the Trustee Act 1925, s.34(2) limits the number of trustees to four in the case of a trust of land (in keeping with the LPA 1925, s.34(2), which limits legal ownership of land to a maximum of four joint tenants).

Upon the death of a trustee or incapacitation of a trust company, new trustees must be appointed. Trustees may retire, but as we will see, the power to retire is typically conditional upon the appointment of a new replacement trustee. The basic reasons that govern a trustee’s power to retire from the trust are obvious. No one should be obliged to serve as a trustee against their will, but on the other hand, retirement may cause expense and inconvenience to the trust (and thus to the rights of beneficiaries) and indeed may endanger the trust if one of two trustees were to retire without replacement.

Trustees are therefore typically required to ensure their replacement before exercising their power to retire. The difference between retirement and removal is that a trustee retires of their own volition, whereas a trustee is removed at the order of another (either by the other trustees, someone else with the power to do so or at the order of the court) when the trustee is unfit to serve as trustee or incapable of doing so. Finally, there may be cases where it is desirable to add a new trustee. This will most obviously be so where the trust was originally constituted with only one human trustee, for the reasons stated above, but may also be desirable in the case where the new trustee will
provide a benefit in terms of judgment. Thus, it may be desirable to appoint a human trustee related to the beneficiaries to act as co-trustee with a trust company in order to assist in the exercise of dispositive discretions, or to add a professional trustee in the case where a family trust is conducted by two family member trustees, to take advantage of the professional's expertise.

14.2 Powers in the trust instrument

**ESSENTIAL READING**

At least one of the following:

- Pettit, Chapter 15: ‘Trustees’, Section 1 ‘Appointment of trustees’.

Powers to appoint or remove trustees or to retire from the trust may be given by the terms of the trust. However, there may be difficulties in framing such powers so that they operate effectively over the lifetime of the trust. It is not uncommon for the settlor of a trust to reserve such powers. But if the settlor should become incapacitated or die, there will be no one with those powers. The same problem would attend the grant of those powers to any named individual. The problem is obvious: the trust may endure for longer than the life of any particular individual, and for that reason, those powers are normally granted to the current trustees, whoever they are (i.e. to office holders rather than to named individuals). The statutory provisions in place essentially provide the same thing (i.e. trustees or their personal representatives if they die in office), so it is common to rely upon them. A further problem can arise if the powers are poorly drafted or conditional (see, for example, *Re Wheeler and De Rochow* [1896] 1 Ch 315), since they may fail to operate properly when the discharge or appointment of trustees is necessary. In practice, the statutory powers of appointment must once again be relied upon.

**FURTHER READING**


**SELF-ASSESSMENT QUESTIONS**

1. What are the circumstances in which a new trustee might need to be appointed?

2. Why are powers provided in the trust instrument to appoint new trustees typically given to the trustees?

14.3 Powers under ss.36 and 39 of the Trustee Act 1925

**ESSENTIAL READING**

At least one of the following:

- Martin, Chapter 17: ‘General principles: capacity; appointment; removal; retirement; control’.
- Pettit, Chapter 15, ‘Trustees’, Section 1 ‘Appointment of trustees’.
The general scheme of statutory powers of appointment is provided by s5.36 and 39 of the Trustee Act 1925. Read them carefully.

Only by dying is a trustee automatically discharged from the trust, and since trustees normally hold the trust assets as joint tenants and not as tenants in common, none of the trust rights will pass to the deceased trustee’s estate. If there is no one able or willing to exercise a power conferred by the trust instrument to appoint a replacement trustee, then the surviving or continuing trustees have that power, and if all the trustees are dead, the personal representatives of the last surviving or continuing trustee have that power: s.36(1). By virtue of s.36(8), a refusing or retiring trustee may appoint their replacement or successor if willing to do so. This can give rise to problems: an appointment is void if a refusing or retiring trustee is willing to participate in the appointment and does not: Re Coates to Parsons (1886) 34 ChD 370.

However, a trustee who is liable to be removed because they fall within one of the grounds for replacement in s.36(1) (i.e. a trustee who is unfit, incapable, or abroad for more than 12 months) may be replaced by the other trustees without the trustee’s participation, even though the trustee may be willing to so participate in their own removal (i.e. otherwise would count as a ‘retiring’ trustee under s.36(8)): Re Stoneham ST[1953] Ch 59.

**FURTHER READING**


**ACTIVITY 14.1**

On what statutory provisions would you rely to:

a. replace one trustee with another
b. add an additional trustee
c. retire as trustee?

**14.4 Powers under s.19 of the Trusts of Land and Appointment of Trustees Act 1996**

**ESSENTIAL READING**

At least one of the following:

- Pettit, Chapter 15: ‘Trustees’, Section 1 ‘Appointment of trustees’.

Recall the principle in *Saunders v Vautier* (Chapter 4) by which a beneficiary who is (or beneficiaries who collectively are) of full age and of sound mind and absolutely entitled under the trust may collapse the trust. In *Re Brockbank* [1948] Ch 206, the court held that this principle did not entitle the beneficiaries to direct the trustees to retire in favour of new trustees they desired. Section 19 of the Trusts of Land and Appointment of Trustees Act 1996 reverses *Re Brockbank* in part.

This power can be excluded by the settlor of a trust under s.21 of the Act.

There is a problem created by s.22(1) of the Act, which reads:

In this Act ‘beneficiary’, in relation to any trust, means any person who under the trust has an interest in property subject to the trust (including a person who has such an interest as a trustee or a personal representative).
Recall from the discussion of the principle of Saunders v Vautier (in Section 4.6.4) that though discretionary beneficiaries may together take advantage of the rule (Stephenson v Barclays Bank Trust Co [1975] 1 WLR 882), they are not regarded as individually having any subsisting beneficial interest (Gartside v IRC [1968] AC 553). It is arguable that s.22 excludes beneficiaries under discretionary trusts from the benefit of s.19.

FURTHER READING

ACTIVITY 14.2
Read Re Brockbank and explain the reasons given for the decision.

14.4.1 Fiduciary nature of the powers

ESSENTIAL READING
- Martin, Chapter 17: ‘General principles: capacity; appointment; removal; retirement; control’.

Review Section 4.2 on the nature of fiduciary obligations. The fiduciary nature of the powers to appoint or remove trustees, or retire from the trust, is straightforward: in exercising these powers, the power-holders are exercising a discretion, one which concerns the operation of the trust, and so will affect the interests of the beneficiaries. Such powers must, therefore, be exercised with the interests of the beneficiaries as paramount.

FURTHER READING

ACTIVITIES 14.3 and 14.4
14.3 Taking into account the fiduciary nature of the powers concerned, explain whether the following exercises of powers of appointment, retirement and removal are valid:

a. Fred and Joe are trustees. They appoint Fred’s sister Stella to replace Joe because Stella is ‘down on her luck’ and could use the trustee’s fees.

b. Simon retires from a discretionary trust because he has grown to hate the beneficiaries and can no longer bear to decide how to distribute funds to them.

c. Sam, the settlor of a trust of shares in his private company, replaces X Co as trustee with Y Co under a power in the instrument because X Co refuses to vote in the way he thinks best for the operation of the company.

d. Arthur retires from the trust in favour of Madge because the majority of beneficiaries ask him to. His co-trustee, Paul, consents to this.

14.4 Review s.19 of the Trusts of Land and Appointment of Trustees Act 1996. Is the power given therein to the beneficiaries a fiduciary power?

14.5 The statutory and inherent jurisdiction of the court

ESSENTIAL READING
At least one of the following:
Equity and trusts

Appointment, retirement and removal of trustees

It is a maxim of equity that ‘a trust will not fail for want of a trustee’. At the same time, no one can be compelled to accept the office of trustee (although people can become resulting or constructive trustees by operation of law without their knowledge or consent). Situations may therefore arise in which there is no one willing or able to exercise a power in the trust instrument or a statutory power to appoint trustees. In such cases, the court must step in. The court, in its inherent jurisdiction to ensure that trusts are carried out, may appoint trustees, but s.41 of the Trustee Act 1925 provides that the court may appoint new trustees where it is ‘expedient’ to do so and it is ‘inexpedient, difficult, or impracticable so to do without the assistance of the court’. Resort to this power of the court should not be made where a person can appoint trustees under a power in the instrument or a statutory power (Re Gibbon’s Trusts (1882) 30 WR 287), though if the existence of a valid power is uncertain resort to the court may properly be made (Re May’s Will Trusts [1941] Ch 109).

Similarly, there may be cases where it is desirable to remove or replace trustees, but there is no one with a power under the trust instrument or a statutory power who is willing or able to do so. Again, the court serves as a last resort. Here, there is no specific statutory provision, and the inherent jurisdiction of the court must be relied upon.

Further reading


Activities 14.5 and 14.6

14.5 Read Re Tempest (1866) LR 1 Ch 485 and describe the principles which guide the court in appointing trustees.

14.6 Read Letterstedt v Broers (1884) 9 App Cas 371 and describe the scope of the court’s inherent jurisdiction to remove trustees and the considerations which guide it when so doing.

14.6 The vesting of the trust rights upon a change of trustee(s)

Essential reading

At least one of the following:

Martin, Chapter 17: ‘General principles: capacity; appointment; removal; retirement; control’, Section 9 ‘Vesting of the trust property in trustees’.


When trustees are appointed, they must acquire the subject matter of the trust, or in the standard terminology, those rights must be vested in them. Similarly, when they are discharged from the trust, they must give up those rights. Typically, there will be more than one person holding the rights on trust. So the newly appointed trustee must become a joint owner of the rights with the continuing trustees, and a retiring trustee must cease to be a joint owner of the rights. So, if A and B are trustees and A retires and is replaced by C, then A and B as joint owners must together transfer the subject matter to B and C as joint owners. If a trustee is removed (i.e. ‘ordered
to retire’) the trustee must act so as to transfer or release the right to the new and continuing trustees. If the trustee refuses to do so, they will be in breach of trust, or if they fail to respond to such an order of the court, will be in contempt.

Section 40 of the Trustee Act 1925 provides that where an appointment is made, the deed by which a trustee is appointed will serve to vest the trust rights in the trustee in so far as a deed can do so. Title to chattels can be transferred by deed, and the deed can be used as a deed of conveyance with respect to unregistered titles to land, and will serve as a transfer document which can be registered in the case of registered titles to land. However, rights which cannot be transferred by deed, such as shares in a private company, must be conveyed in the appropriate way.

Partly because of the inconvenience and cost of re-vesting the rights upon a change of trusteeship, large trusts with boards of trustees (such as large charities or pension funds) which may change the composition of the set of trustees on a regular basis, often have managing trustees and a custodian trustee. The custodian trustee (always a company) is a bare trustee that simply holds the trust rights and follows the direction of its beneficiaries, but in this case those beneficiaries are the managing trustees who in turn hold their equitable interests in trust for the real beneficiaries. The managing trustees are the real trustees because they really operate the trust via their directions to the custodian trustee. When a managing trustee is discharged or a new one appointed, this can be done by deed and no re-vesting of the underlying trust rights is required, for they remain with the custodian.

**FURTHER READING**


**SELF-ASSESSMENT QUESTIONS**

1. Why is the presence of managing and custodian trustees in a trust relevant to the issue of the appointment and discharge of trustees?
2. How did the Trusts of Land and Appointment of Trustees Act 1996 change the law concerning the appointment and discharge of trustees?

**SAMPLE EXAMINATION QUESTIONS**

**Question 1** By his will, a testator, who died last year, appointed Tick and Tock to be his executors and trustees and left his residuary estate, consisting of freehold and leasehold estates, company shares and bearer securities, upon trust for his three sisters in equal shares absolutely. The three sisters are all of full age and desire the trust to continue. Tock has been living in Spain for the last six weeks, and though he intends to remain ordinarily resident in England, he has indicated that he will spend much of his time in Spain in the future. Tick wishes to appoint Little in place of Tock, but the three sisters either want Tock to remain or Large to be appointed in his place. Advise Tick.

**Question 2** Discuss the reasons for the various statutory provisions which concern powers to appoint and discharge trustees and explain the considerations governing their operation.

**ADVICE ON ANSWERING THE QUESTIONS**

**Question 1** This question raises four main issues:

i. Who has the power to decide on the person to be appointed?

ii. By whom must the appointment be made?

iii. By what method must the appointment be made?

iv. How will the trust rights be vested in the trustees?
i. Concerns who, in the circumstances, has a discretion to decide upon appointments, and if more than one, which has priority. If there was a power in the trust instrument, that would have priority (s. 36(1)(a) Trustee Act 1925), but there appears to be none. Therefore, Tick and Tock will have a power under s.36(1)(b). But the three sisters also have a power by virtue of s.19 Trusts of Land and Appointment of Trustees Act 1996 (as they are fixed interest beneficiaries there is no s.22(1) problem) to direct the trustees to retire and/or appoint new trustees according to their written direction.

ii. Whether in response to a written direction from the sisters, or acting under s.36(1), the appointment or discharge must be made by Tick and Tock. If one is unwilling to act, his replacement under s.36(1) can be made by the other. Tock has not been out of the country for 12 months so cannot be removed unilaterally by Tick.

iii. Any appointment or discharge must be made by deed.

iv. The vesting of trust rights in new trustees must occur by way of the appropriate modes of transfer of the rights in question, except where it is provided that the deed of appointment or discharge serves to divest the discharged trustee and vest the new trustee with the trust rights (s.40). In this case, the transfer of freehold and leasehold and freehold estates (over seven years) will require registration of the deed as a transfer document at the Land Registry. The shares must be transferred separately, either by transfer form and registration by the company, or via the CREST system. Bearer securities are transferred by delivery.

**Question 2** This question involves two parts:

1. An explanation of ss.36, 39, and 41 of the Trustee Act 1925, and of s.19 of the Trusts of Land and Appointment of Trustees Act 1996; with regard to ss.36 and 39, it should be explained how they relate to powers provided in the trust instrument (if any) and to the powers of the court. With respect to s.41, the background of the inherent jurisdiction of the court should be explained. With s.19, the background of the previous law under Re Brockbank [1948] Ch 206 and the possible uncertainty of its application to discretionary and similar trusts should be described.

2. Regarding the considerations which go into the exercise of powers of appointment, it should be noted that they are fiduciary powers when exercised by trustees, and the best interests of the beneficiaries should be the only considerations. With respect to the court, similar considerations apply (Re Tempest; Letterstedt v Broers); with respect to the beneficiaries’ exercise of their rights under s.19, there would appear to be no scope for any fiduciary obligation, but beneficiaries should be wary of using the threat of removal to ‘micro-manage’ the trust, making the trustee act to their order. In such circumstances, they might be regarded as having established an agency relationship, with the trustee simply doing their bidding.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>I can give examples of circumstances in which the appointment, retirement, or removal of a trustee is desirable or necessary.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain why the statutory powers of appointment, retirement, and removal of trustees are generally relied upon in preference to powers in the trust instrument or the jurisdiction of the court.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain how the statutory powers found in ss.36 and 39 of the Trustee Act 1925 and s.19 of the Trusts of Land and Appointment of Trustees Act 1996 work, and explain the extent to which they are fiduciary powers.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain the court’s powers in relation to the appointment and removal of trustees.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain when, why, and how rights held on trust are dealt with upon a change of trustees.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>14.1 The appointment, retirement, and removal of trustees in outline</td>
<td></td>
</tr>
<tr>
<td>14.2 Powers in the trust instrument</td>
<td></td>
</tr>
<tr>
<td>14.3 Powers under ss.36 and 39 of the Trustee Act 1925</td>
<td></td>
</tr>
<tr>
<td>14.4 Powers under s.19 of the Trusts of Land and Appointment of Trustees Act 1996</td>
<td></td>
</tr>
<tr>
<td>14.5 The statutory and inherent jurisdiction of the court</td>
<td></td>
</tr>
<tr>
<td>14.6 The vesting of the trust rights upon a change of trustee(s)</td>
<td></td>
</tr>
</tbody>
</table>
15 Variation of trusts

Contents

Introduction ......................................................... 162

15.1 The principle in *Saunders v Vautier* ................................. 163

15.2 The grant of administrative powers: Trustee Act 1925, s.57 .......... 164

15.3 The variation of beneficial interests: Variation of Trusts Act 1958 .... 164

Reflect and review .................................................... 168
Introduction

Many trusts last for a long time. Family trusts are typically designed to distribute the settlor’s wealth over several generations. Because circumstances may change, in particular the tax environment in which a trust operates, the original terms of the trust may give rise to difficulties. In such cases, variation of the terms of the trust may be desirable. Variations must benefit all the beneficiaries under the trust, or at least not disadvantage any of them, and it is this concern which has generated the current legal regime. As we will see, the law’s answer to the problem, provided by case law and statute, is essentially to require each beneficiary who is sui juris (i.e. of full age and sound mind) to consent to a proposed variation, while the court will consent on behalf of those who are not sui juris. However, the court will not do so unless it is convinced that a genuine benefit has been conferred on the incapable beneficiaries by the proposed variation.

Essential reading

- Penner, Chapter 10: ‘The trust up and running’, paras 10.66–10.77 (‘Variation of trusts’).

Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- explain how the principle in Saunders v Vautier is relevant to the variation of trusts
- describe the scope of the court’s inherent jurisdiction to vary trusts and the problems that arise in consequence
- explain the operation of s.57 of the Trustee Act 1925
- explain the operation of the Variation of Trusts Act 1958.
15.1 The principle in *Saunders v Vautier*

Review the principle in *Saunders v Vautier* (1841) in Section 4.6. The general formulation of the principle is typically that a beneficiary who is *sui juris* and absolutely entitled under the trust may collapse the trust (i.e. ‘call’ for the trust rights to be conveyed to himself). The same principle applies to a group of beneficiaries if they can all agree to do so. By the same token, *sui juris* beneficiaries can instead consent to a variation of trusts (i.e. a change in the terms upon which the trust rights are held).

15.1.1 Limitations on the principle

There are two limitations on the principle.

The first arises out of the case of *Re Brockbank* [1948] Ch 206, which (as we saw in Chapter 14) lays down the rule that the beneficiaries, though *sui juris*, are not entitled to direct the trustees in the exercise of their discretions under the trust. They can collapse the trust or insist upon a variation, but are not entitled to ‘micro-manage’ the trust by themselves, taking the decisions that a trustee is authorised to take to give effect to the trust. That would completely defeat the point of there being a trust.

The second limitation is pertinent to this chapter. Only *sui juris* beneficiaries can consent to a variation. Under-age beneficiaries and those who are otherwise unable to act for themselves (e.g. the mentally disabled) cannot consent. Since many trusts are intergenerational, there will often be minor beneficiaries who cannot consent to a proposed variation even if it was clearly in their interests. There will often also be the possibility of if potential beneficiaries yet to be born into the class of beneficiaries. The Variation of Trusts Act 1958 has largely overcome these limitations.

**Activity 15.1**

a. What is the principle in *Saunders v Vautier* and how does it apply to the issue of the variation of trusts?

b. What limitation of the *Saunders v Vautier* principle makes it an ineffective basis for varying trusts in many cases?

No feedback provided.

15.1.2 The inherent jurisdiction of the court

As we have seen throughout this guide, the Court of Equity has an inherent supervisory jurisdiction over trusts. Where a proposed variation is for the benefit of all the beneficiaries, including those not *sui juris*, does the court have an inherent jurisdiction to consent on behalf of those not *sui juris*? This issue was considered by the House of Lords in *Chapman v Chapman* [1954] UKHL 1, [1954] AC 429. Although the speeches in that case seem to indicate that a practice had developed in which Chancery judges (in chambers) would approve of certain variations on behalf of those not *sui juris*, the House firmly rejected the existence of any such jurisdiction.

The inherent jurisdiction of the Court is limited to:

1. granting additional administrative powers to the trustee in emergencies (i.e. situations where the limitations in the trust instrument upon the investment or management of the trust assets jeopardise the functioning of the trust), and
2. sanctioning maintenance payments to a beneficiary otherwise not provided for.

The court also has the jurisdiction to sanction a compromise on behalf of minor beneficiaries where there was a dispute as to the rights of beneficiaries under a trust. This last jurisdiction is best seen not as a jurisdiction to sanction a variation of the rights of beneficiaries, but to sanction an agreement as to what those rights actually are. However, by extending this jurisdiction to sanction a compromise, Chancery judges had considered themselves empowered to consent to certain variations in the beneficial interests of those not *sui juris* under the trust, and it was this practice that the House held to be invalid in *Chapman*. In the wake of this decision, the Variation of
Trusts Act 1958 was passed, which provided the court with the very power the House said it lacked.

**Activity 15.2**


How do the two judges’ views differ as to the inherent jurisdiction of the court in the matter of trusts? Whose views do you prefer?

### 15.2 The grant of administrative powers: Trustee Act 1925, s.57

This provision extends the court’s power to confer upon trustees additional administrative powers to cases where in the opinion of the court it is expedient to do so. Thus, by virtue of the statute, the situation need not be an emergency, to which cases the House in *Chapman v Chapman* said the inherent jurisdiction was confined. Use of s.57 was made in *Trustees of the British Museum v A-G* [1984] 1 WLR 418, where the trustees of the British Museum successfully persuaded the court to extend their powers of investment so that they would continue to amass the funds necessary to enhance the museum’s collection by purchases from time to time.

**Activity 15.3**

Make a short spoken statement on why the enlargement of investment powers in *Trustees of the British Museum v A-G* could be authorised by the court under s.57 of the Trustee Act 1925 but not under the court’s inherent jurisdiction.

**Summary**

As a corollary of the principle in *Saunders v Vautier*, *sui juris* beneficiaries can consent to any variation of trust, but those under-age or otherwise incompetent cannot. The court’s inherent jurisdiction is limited to the grant of further administrative powers in cases of ‘emergency’ powers, though s.57 of the Trustee Act 1925 enlarges the power to any case where the enlargement of powers is expedient, and, with respect to dispositive provisions of a trust, to allowing maintenance payments. The court can consent to a compromise of rights, but this is not properly seen as a power to vary dispositive trust provisions. *Chapman* establishes that the court has no inherent jurisdiction to consent to the variation of trust on behalf of those beneficiaries who are not *sui juris*, however much in their beneficiaries’ interests such a variation might be.

### 15.3 The variation of beneficial interests: Variation of Trusts Act 1958

To a large extent, the Variation of Trusts Act 1958 reversed the decision in *Chapman*, empowering the court to consent to a variation on behalf of beneficiaries who are not *sui juris*.

The Act appears merely to authorise the court to approve a variation of the trust on behalf of ascertained beneficiaries. The remaining beneficiaries (essentially all those who are *sui juris* and ascertainable) must give their own consent if they are to be bound by the variation (*IRC v Holmden* [1968] AC 685; *Re Holt’s ST* [1969] 1 Ch 100). In earlier cases, it was assumed that the court would only make an order of variation when all the *sui juris* beneficiaries consented and the court was able to consent on behalf of the others. The difference is substantial, for arguably, if the *sui juris* beneficiaries’ consent to the variation agreement effects the variation of the trust, rather than the court’s order, they ‘dispose’ of their equitable interests under the trust and must do so in writing to comply with s.53(1)(c) of the LPA 1925 (see Section 7.2). If this were indeed the law, variations would be more inconvenient and many
past variations would be void. In *Re Holt’s ST*, Megarry J held that although, from one perspective, the *sui juris* beneficiaries ‘dispose’ of their equitable interests under the trust when they consent to the variation, the court’s declared consent on behalf of the other beneficiaries is sufficient to make the variation effective, even in the absence of writing.

The court may give its approval on behalf of the classes of beneficiaries set out in s.1 of the Act. Section 1(1)(a) comprises minors and others lacking capacity to consent. Section 1(1)(b) is difficult to interpret, but *Re Suffert’s Settlement* [1961] Ch 1 and *Re Moncrieff’s ST* [1962] 1 WLR 1344 hold that the court may approve on behalf of those who may in the future become entitled under a trust, except for ascertainable (i.e. identifiable) persons who would become entitled on the happening of a single event – such persons, if *sui juris*, must give their own consent. For example, if Paul, aged 25 and mentally competent, will become entitled to an interest under the trust if his widowed mother remarries, then he must consent to any proposed variation.

The court cannot consent for him. Section 1(1)(c) comprises the unborn, while s.1(1)(d) comprises those who would become beneficiaries under the discretionary trust following the end of the principal trust under a protective trust (see Section 3.3).

The court must be satisfied that any variation benefits each member of classes (a), (b), or (c) before giving its approval on their behalf. Typically, the benefit will be financial, usually as a result of tax savings, but financial advantage is neither sufficient (*Re Weston’s Settlement* [1969] 1 Ch 223) nor necessary (*Re Remnant’s ST* [1970] Ch 560). Given the limited predictability of future events, it may be uncertain whether a proposed variation will in fact result in a benefit to someone on whose behalf the court consents, but the court will consent to a variation if in so doing it only takes risks which an adult would be prepared to take (*Re Cohen’s WT* [1959] 1 WLR 865).

An important question is the extent to which, if at all, the court should have regard to the settlor’s intentions. Clearly, the court may override the settlor’s plan where it is satisfied that the variation is of benefit to the beneficiaries (*Re Remnant’s ST*). More recently, the Court of Appeal in *Goulding v James* [1997] 2 All ER 239 affirmed the basic principle (from which *Re Steed’s WT* [1960] Ch 407 appeared to have deviated) that the settlor’s intentions are relevant only in so far as they assist the court in determining what is of benefit to the beneficiaries on behalf of whom the court consents. The court is not bound by the settlor’s intention and neither are the *sui juris* beneficiaries. This principle of English trusts law stands in contrast to the ‘material purpose’ doctrine prevalent in many USA jurisdictions and which has been imported by statute elsewhere. Under this doctrine, no variation of a trust, even if all the beneficiaries are *sui juris*, may occur if a ‘material purpose’ of the settlor in creating the trust may yet be fulfilled. This doctrine detracts from the principle of *Saunders v Vautier* and has so far received no judicial attention in this country.

**Summary**

The Variation of Trusts Act 1958 allows the court to consent to a variation of trust on behalf of beneficiaries who are not *sui juris* and on behalf of potential future beneficiaries who are unborn or unascertainable, if the variation would be for their benefit (except for beneficiaries under s.1(1)(d)). Benefit is more broadly construed than ‘financial’ benefit, though financial benefits (in particular the saving of tax) are typical, and reasonable risks as to the future may be consented to. In general, the court is not bound in any way to observe the settlor’s motives, purposes, or expectations for the trust, though the settlor’s views may be relevant in determining the extent of the benefit any proposed variation would have for the beneficiaries for whom the court consents.

**Activity 15.4**

Although facilitative and generally regarded as beneficial, the Act has not disposed of all problems in this area. Read the case of *Knocker v Youle* [1986] 1 WLR 934 and explain why the Act may give rise to substantial inconvenience.
**ESSENTIAL READING**

At least one of the following:

- Pettit, Chapter 22: ‘Variation of trusts’.
- Oakley, Chapter 21: ‘Variation of trusts’.
- Martin, Chapter 22: ‘Variation of trusts’.

**FURTHER READING**

- Hayton & Mitchell, Chapter 7: ‘Variation and termination of trusts’, Section 4 ‘Judicial variation of trusts’.

**SAMPLE EXAMINATION QUESTIONS**

**Question 1**

Either the settlor’s intentions should prevail, in which case no variation of a trust should be allowed, or the foundational equitable principle that the trust rights in effect belong to the beneficiaries, in which case the trust should be varied in whatever way is most beneficial to them.’

Discuss.

**Question 2**

Under the trusts of a settlement of personal property, a trust fund currently worth £250,000 is held by the trustees upon trust to pay the income thereof to Amy upon a protective trust (under the Trustee Act 1925, s.33) for her life and subject thereto upon trust for such of Amy’s children as she shall by deed appoint and in default of such appointment on trust for such of Amy’s children as shall attain the age of 21 and if more than one in equal shares.

Amy is 56 years of age and has two children, Janet aged 20 and John aged 18. Amy, Janet, and John would like to divide up the capital of the trust fund amongst themselves.

Advise them whether this may be done, and if so, what steps they would need to take.

**Question 3**

What differences are apparent in the law’s attitude to variations of administrative provisions and dispositive provisions in trusts? Are these differences justifiable?

**ADVICE ON ANSWERING THE QUESTIONS**

**Question 1**

This question poses much the same issue as that faced by the court in *Chapman*, and the alternative views appear to mirror in large part those expressed by Lord Simonds LC and Denning LJ respectively, and a good answer would make reference to them. The question goes beyond the role of the court’s inherent jurisdiction, raising the stronger claim, not just about whether a court should act to vary a trust to benefit the beneficiaries, but whether anyone, in particular the *sui juris* beneficiaries, should be able to do so based on their *Saunders v Vautier* rights. Should the law recognise something akin to the ‘material purpose’ doctrine in the US, which cuts those rights down?

**Question 2**

The first thing to do here is to sort out the interests under the trust. Under the protective trust, Amy is currently the income beneficiary (‘life tenant’) under the trust. If that trust were to come to an end because she attempted to assign her interest to another or was declared bankrupt, the secondary trust would arise under which (by virtue of s.33(ii)(a)) Amy, any present or future (see *Re Steed’s WT*) husband of hers, Janet and John would each be beneficiaries. Following Amy’s death, the fund would go in equal shares to Janet, to John if he were to reach 21, and to any other child Amy might yet have who reached 21. If this was the entire structure of the trust, Amy, Janet and John, all being *sui juris*, would have to apply for the court under the Variation of Trusts Act 1958 to consent on behalf of any husband of Amy (s.1(1)(d)), and on behalf of any unborn children she might yet have (s.1(1)(c)). The variation need not be of benefit to any husband of Amy, but a benefit must be provided for the possible unborn child (s.1(1), proviso), and so a simple division of the funds between them would not go through. However, the problem of the unborn child could be avoided if Amy were
to appoint the capital interest to specific children of hers by deed. She could therefore appoint the capital to Janet and John, following which only they and any husband of hers under the protective trust are beneficiaries, and they can propose to vary the trust so as to give themselves equal shares and apply to the court under the Variation of Trusts Act 1958 to consent on behalf of any husband of Amy, for whom the court need find no benefit under the variation.

**Question 3** The first point your answer should capture is that according to *Chapman v Chapman* the inherent jurisdiction of the court is limited to that of varying the administrative provisions of trusts, and then only in restricted circumstances. The administrative/dispositive split is mirrored in the separate legislation dealing with variations, s.57 of the Trustee Act 1925 and the Variation of Trusts Act 1958. There is an arguably sound rationale for this difference in attitude. In *Chapman*, the House of Lords said that for the court to vary the dispositive terms of a trust would be to replace their own distribution of bounty for the settlor’s, a power which would unjustifiably interfere with the settlor’s right to give their assets to whomever they wished in whatever shares and on whatever conditions they wished. Varying administrative provisions can be portrayed as merely providing better means to carry out what is the same trust in substance. On the other hand, the stark division does give rise to some inconveniences, for example the *Knocker v Youle* problem, where arguably the law extends too much care over the variation of dispositive provisions which may have little or no practical effect.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>I can explain how the principle in <em>Saunders v Vautier</em> is relevant to the variation of trusts.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can describe the scope of the court’s inherent jurisdiction to vary trusts and the problems that arise in consequence.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain the operation of s.57 of the Trustee Act 1925.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain the operation of the Variation of Trusts Act 1958.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>15.1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>15.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>15.3</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Introduction

A trust can be breached in different ways. For example, a trustee:

- might fail to carry out the terms of the trust, for example by failing to pay a beneficiary what they are due
- might enter into transactions with the trust rights that are prohibited by the trust instrument or by the general law.

The general rule is that trustees are strictly liable for any loss caused by their breach of trust, that is, they are liable to pay money out of their own pockets to make up any loss to the trust funds caused by their breach of duty. It is vital to realise that this liability is only personal. If a trustee is insolvent, the beneficiaries’ claim that the trustee make good the loss will generally be not worth pursuing.

Trustees are not necessarily liable for the breaches of their co-trustees. Trustees may be relieved of liability by an exemption clause in the trust instrument or by the court in certain circumstances.

Third parties (i.e. non-trustees) may also incur personal liabilities when a trust has been breached. They may be liable if they were accessories to the breach of trust or received trust assets or their traceable proceeds (see Chapter 19: ‘Constructive trusts II’) in breach of trust. In addition, they will be liable to reconvey any trust assets received in breach of trust, unless they are protected by the defence of *bona fide* purchaser for value without notice or similar immunity provided by land registration statutes.

**Essential reading**

- Chapter 4 of this subject guide, Sections 4.1–4.1.3.

**Learning outcomes**

By the end of this chapter and the relevant reading, you should be able to:

- describe the various ways in which a trust can be breached
- explain the various personal and proprietary rights that the beneficiaries may have against trustees and third parties when a trust is breached
- explain the process of ‘surcharging’ or ‘falsifying’ the trust accounts
- explain the liability of trustees for breach of trust among themselves, and the consequences of a beneficiary’s consent to a breach of trust
- explain and apply s.61 of the Trustee Act 1925 and the law governing trustee exemption clauses
- explain and apply the tests which govern third-party liability for assisting in a breach of trust and receiving trust property.
16.1 Liability of a trustee for breach of trust

16.1.1 Personal and proprietary rights

Perhaps the most straightforward breach of trust is the case where the trustee fails to carry out a term of the trust, for example, to invest the trust property, or to dispose of the trust rights according to the terms of the trust.

In such cases, the beneficiaries can apply to the court, which will order the trustee to carry out their duties. Perhaps more effectively, the beneficiary may have the power or may seek the court’s assistance to replace the defaulting trustee with one who will carry out the trust (see Chapter 14). The remedy here is essentially an order for performance of the trust. The court will either order the trustee to carry out their duties on pain of being in contempt of court or replace them with a trustee willing so to do. The liability of the trustee to such an order is clearly personal, to deal with the trustee’s nonfeasance (i.e. failure to act).

Personal liability indicates the case where a trustee is liable to pay money out of their own pocket to compensate for a loss to the trust, whereas ‘proprietary liability’ indicates the case where the beneficiaries can claim that some specific asset they would otherwise hold outright is held for them on trust. The same distinction applies to the liability of third parties, who may be personally liable for assisting a breach of trust or for receiving rights dissipated in breach of trust (i.e. be required to pay out money from their own pocket to restore a loss to the trust) or may be proprietary liable (i.e. hold some right, either the trust right or its traceable substitute, in trust to be transferred to the proper trustees).

16.1.2 Falsifying and surcharging the trust account

A basic division can be made between breaches of trust where the trust account can be ‘falsified’ and those where it can be ‘surcharged’. This is an odd use of the word falsify, not to mean ‘to make false’ as it usually does, but ‘declare to be false’. The terminology of ‘falsifying’ and ‘surcharging’ the trust account follows from the trustee’s primary duty to keep trust accounts. Because the trust assets often constitute a fund which changes over time (e.g. as they are invested in various ways, income is added to the trust and payments are made to beneficiaries) the trustees must keep track of the rights coming into and going out of the trust fund. They must maintain records of these transactions, such records being the ‘trust account’.

Falsifying

When a beneficiary sues a trustee for breach of trust, this is traditionally framed as calling for an account. The beneficiaries apply to court asking the trustees to account for what they have done with the trust rights. Where the trustees have made an unauthorised transfer of trust assets (e.g. by making an unauthorised investment or paying someone who is not a proper beneficiary of the trust) the beneficiaries are entitled to falsify the account in respect of that particular transaction. Where possible, the trustees can remedy the breach by reversing the transaction to restore the trust. For example, they can remedy an unauthorised sale of land previously held on trust by re-purchasing it, making up any difference in price from their own pockets. If they cannot reverse the transaction (e.g. where money was paid away to a non-beneficiary who became insolvent), the trustees will be personally liable to pay an equivalent sum (plus interest) from their own pockets into the trust.

Surcharging

The beneficiaries surcharge the account where the trust fund has less value than it should, but not because the trustee entered into any particular, identifiable transaction which can be falsified. Two examples of this kind of breach are:

1. where trustees negligently invest the trust fund so that it is worth less than it would be if sufficient care had been taken to maintain and enhance its value
2. where trustees fail to insure trust assets, which are then damaged, destroyed or stolen.

In both these examples, there is no particular unauthorised transfer that can be falsified. The real problem is the failure to enter a transaction that should have taken place (to make a better investment or purchase insurance). The trustees are personally liable to make good the loss from their own pockets. The trust account is surcharged to add the value that should have been received either from proper investments or from insurance proceeds. Note that in cases where the trust is surcharged, there is no way to restore the trust by reversing any particular transaction, and so the liability of the trustee can only be personal.

**Strict liability**

It is important to note that in most of the above cases, the liability of the trustees is strict. Negligent investment apart, the law does not ask whether the trustees breached the trust honestly, negligently or intentionally. They are liable for the breach regardless, in just the same way as a contracting party is strictly liable for breach of contract. However, there are certain circumstances in which trustees may escape liability for breaches they have committed. Principally, these are where (a) the beneficiaries consent to the breach, (b) the trust instrument contains a clause exempting the trustees from liability or (c) the court relieves the trustees of liability. This is discussed further below under s.61 of the Trustee Act 1925.

In all the above cases, one identifies a breach of trust by showing that a term of the trust or a general duty imposed on trustees has been breached. An entirely different circumstance in which trustees may be liable for breach is where they are in breach of a fiduciary obligation owed to the beneficiaries. This is different from breach of trust because fiduciary obligations apply not only to trustees but to other legal actors, such as agents, company directors and solicitors. Fiduciary obligations, in short, are not the same thing as trust obligations, although trustees typically have both. For this reason, fiduciary obligations will be dealt with separately, in the next chapter.

**Activities 16.1–16.3**

16.1 Explain the difference between cases in which (a) the trust is specifically enforced, (b) the trustee is personally liable for breach of trust and (c) a trustee is proprietarily liable in the case of a breach of trust.

16.2 What is the difference between falsifying and surcharging the trust account?

16.3 Give examples of breaches of trust and identify whether this would entitle the beneficiaries to:
   a. falsify the account
   b. surcharge the account.

**16.2 Personal liability of a trustee for breach of trust**

A trustee (or a third party, for that matter) may be liable to pay money out of their own pocket to restore a loss caused to the trust, either by an unauthorised transaction which can be falsified or by a failure to acquire assets or value for which the account can be surcharged. This liability is by and large the counterpart in equity to the liability at common law to pay money damages to compensate for a loss caused by a tort or breach of contract. In both cases there was a breach of duty, that breach gave rise to a loss quantifiable in money, and the duty-holder was liable to pay money compensation for the loss that resulted. Unfortunately, the peculiar terminology of equity has obscured the basic simplicity of what is going on.
16.2.1 Liability to account and equitable compensation

The trustees' primary duty is to keep the trust rights separate from their own and to keep the trust accounts. Therefore, the liability of trustees to compensate the beneficiaries (by paying money into the trust to restore the value of any losses the trust fund suffered due to their breach) is generally referred to as a liability to account. Even in the case of a third party who is personally liable to restore the trust, for example because they dishonestly assisted the trustee in carrying out a breach which caused a loss, their liability is often framed as a liability to account 'as if they were a trustee'. In both cases, the liability is in reality a liability to compensate for loss by payment of money. Therefore, it would be perfectly sensible to say that these are cases of equitable compensation.

Historically, however, the term 'equitable compensation' has not been given this broad reading, but refers to cases where a claimant is compensated directly by a money payment (i.e. the payment is not made to restore the value of a trust fund). This can happen in the case of a breach of trust. In *Target Holdings Ltd v Redferns* [1995] UKHL 10, [1996] AC 422, a solicitor held funds obtained from a lender on trust to complete a purchase of land and obtain a mortgage on the land in the lender's favour. It was alleged that the solicitor helped defraud the mortgage lender by entering into a series of land transactions not sanctioned by the lender. By the time of trial, there was no purpose to be served in restoring the trust (i.e. requiring the solicitor to pay his own funds into a new trust to be held for the lender). The lender wanted its losses under the land transactions carried out in breach of trust compensated, and sued the solicitor for a payment to it directly. In short, the lender claimed equitable compensation from the solicitor (i.e. a direct payment to compensate it for the loss it had suffered).

In *AIB Group (UK) plc v Mark Redler & Co* [2014] UKSC 58, [2014] 3 WLR 1367, the Supreme Court of Appeal followed *Target Holdings*, in a case involving a similar legal problem. The defendant solicitors had disbursed £3.3 million in breach of trust, but were not liable to account for the entire amount. They were liable only for the actual loss of £300,000 caused by the breach. Lord Toulson said at [76],

Equitable compensation and common law damages are remedies based on separate legal obligations. What has to be identified in each case is the content of any relevant obligation and the consequences of its breach. On the facts of the present case, the cost of restoring what the bank lost as a result of the solicitors' breach of trust comes to the same as the loss caused by the solicitors' breach of contract and negligence.

Equitable compensation, then, appears to refer to cases where the defendant is liable in equity to pay an individual directly in order to compensate that person for a loss caused by the defendant's breach of an equitable duty. This can occur in cases where there is no trust or breach of trust, for example, where a fiduciary obligation is breached. Those cases will be dealt with in Chapter 17.

16.2.2 Personal liability and causation of loss

Trustees will only be liable for a loss to the trust fund or to a beneficiary if the loss has been caused by their breach of duty. For example, trustees will not be liable if the trust fund loses value just because there is a general decline in the market value of the trust assets (*Re Chapman* [1896] 2 Ch 763). The loss must flow from their breach of trust. This raises issues of causation. The beneficiaries must show that the loss was caused by the breach.

There are two sorts of situation in which causation for loss must be considered: (1) where the account is falsified and (2) where the account is surcharged. (Losses caused by a trustee breaching a fiduciary obligation to the beneficiaries will be discussed in the next chapter.)
Account falsified

When an account is falsified, the beneficiaries claim that a transfer of trust assets was in breach of trust. The loss caused by the breach in such a case is straightforward. The trust no longer has a right it once did, and the trustee is bound either to reverse the transaction, or to pay money to put the trust in the position it would have been in had the right been retained (Target Holdings). So, for example, where the trustee in breach of trust sold shares for £50,000 which are now worth £80,000 (the date at which the loss is to be valued is the date of trial (see Nocton v Lord Ashburton [1914] AC 932 and Target Holdings), the trustee must either purchase shares to replace those lost, or if that is not possible, pay £30,000 into the trust (plus the value of any dividends that would have been received if the shares had been kept, but minus any interest earned on the £50,000 actually received from their sale). The loss caused is clearly the decline in value of the trust rights caused by the falsifiable transaction. The amount of loss is purely a calculation concerning the value of rights. In certain respects, the valuation of the loss departs from the principles which would be applicable at common law, in the sense that the trustees may be required to pay money to the trust which would put the trust in a better position than if the breach had never occurred.

It should be noted that many of the relevant cases were decided in the 19th century, and a court today might be more willing to apply by analogy the common law tests of remoteness of damage and causation, thereby minimising the trustee’s liability for more or less imaginary values which the trust might have obtained but for the breach (see Bristol and West Building Society v Mathew [1996] EWCA Civ 533, [1998] Ch 1). In Target Holdings, Lord Browne-Wilkinson maintained that the test for causation of loss in a case of equitable compensation remained different from that of the common law with the former designed: ‘to make good a loss in fact suffered by the beneficiaries, which using hindsight and common sense, can be seen to have been caused by the breach’. It is not clear that this way of putting things distinguishes an approach which materially differs from what the common law rules of causation aim to achieve, but it was approved by the Supreme Court in AIB Group (UK) plc v Mark Redler & Co, in which Lord Reed said at [136]:

> It follows that the liability of a trustee for breach of trust, even where the trust arises in the context of a commercial transaction which is otherwise regulated by contract, is not generally the same as a liability in damages for tort or breach of contract. Of course, the aim of equitable compensation is to compensate: that is to say, to provide a monetary equivalent of what has been lost as a result of a breach of duty. At that level of generality, it has the same aim as most awards of damages for tort or breach of contract. Equally, since the concept of loss necessarily involves the concept of causation ... there are some structural similarities between the assessment of equitable compensation and the assessment of common law damages.

Account surcharged

Where the account is surcharged, issues of causation are somewhat different. Recall the case of Nestle v National Westminster Bank (Chapter 4, Activity 4.7), where the plaintiff claimed that the trustees (who were clearly in breach of trust for failing to seek advice about the scope of the trust’s investment clause and therefore made investments in breach of trust) caused a loss in the capital value of the trust fund. The plaintiff therefore surcharged the account, claiming that the trustees would have produced much greater capital growth in the trust fund if they had made their investment decisions properly. She lost. While it was clear that the trustees acted in breach, the plaintiff had not shown that the low capital growth was due to the trustee’s breach, because even if they had known the true scope of their investment powers, it was not shown that they would have obtained greater capital growth given the standards of professional investment prevailing at the time.

Thus, unlike falsification of the account, when the account is surcharged showing whether a breach caused a loss is not a simple matter of asset valuation. It involves a genuine requirement to show that the loss flowed from the breach of trust and not
from some other factor, such as in Nestle, the standard investment practices at the
time. In such cases, it has been said that the common law principles of causation,
remoteness of damages, and measure of damages, should be applied by analogy
(Bristol & West Building Society v Mothew [1998] Ch 1, per Millett LJ).

**ACTIVITY 16.4**

Read AIB Group (UK) plc v Mark Redler & Co [2014] UKSC 58, [2014] 3 WLR 1367 and
explain the decision, in particular the way in which the court applied the rules of
causation which govern the award of equitable compensation.

**Summary**

A trustee or third party may be liable to restore a loss caused to the trust. This liability
is the counterpart in equity of the liability at common law to pay damages for a
tort or breach of contract. Liability to account is the liability of the trustee or a third
party to compensate the beneficiaries to restore any loss to the trust by making a
money payment into the account. Equitable compensation refers to cases where the
defendant has a liability in equity to pay an individual directly in order to compensate
that person for a loss caused by the defendant’s breach of an equitable duty. This
occurs in more than just breach of trust cases, for example, where the defendant
breaches a fiduciary duty causing loss.

A trustee is only liable for a loss to the trust fund or to a beneficiary if the loss has been
caused by the trustee’s breach of trust. Consequently this raises the issue of causation.
Two situations must be considered:

1. Where the account is falsified, the trust no longer had a particular asset and the
   trustee is bound either to reverse the transaction, or to pay money into the trust
to restore the value of the trust had the asset been retained. Thus, the issue of
causation only concerns fluctuations in the value of specific assets.

2. Where the account is surcharged, the claimant must show that the loss flowed
   from the breach and not from some other factor. As a consequence, the common
law principles of causation, remoteness of damages, and measure of damages
should be applied by analogy.

**16.3 Liability of trustees inter se**

**16.3.1 Joint and several liability**

Where there is more than one trustee, the question of liability among trustees (inter
se) arises. The background principle is that trustees must carry out the trust together,
and because they will normally hold those rights as joint tenants, must all participate
where a transaction involves dealing with the trust assets. The law does not recognise
the principle of a ‘sleeping trustee’, who does nothing in the administration of the
trust (Bahin v Hughes (1886) 31 Ch D 390). Trustees are jointly and severally liable when
they act together, or ought to have acted together, in doing anything which they
should not have done, or failing to do what they should have done. Nevertheless,
where a breach is committed by a trustee clearly acting alone, where for example one
trustee misappropriates some of the trust rights, their co-trustees will not be liable.

Where trustees are together liable, the court may, under the Civil Liability
(Contribution) Act 1978, apportion liability amongst them according to their individual
degree of fault. One trustee may also seek an indemnity from another trustee (i.e.
may require the other trustee to pay their share of equitable compensation) when
the latter alone misappropriated trust rights, or when the latter is a solicitor who
exercised a controlling influence over the trust, and thus is essentially responsible for
the breach (Bahin v Hughes).
16.3.2 Consent of beneficiaries

A beneficiary who is *sui juris* (i.e. of full age and of sound mind) who may consent to a trustee acting in a way which departs from the terms of the trust. If all the beneficiaries are *sui juris*, and they all consent to an action which departs from the trust terms, there is no breach of trust. For genuine consent, the beneficiaries must be fully informed of the relevant facts, though they need not know the exact nature of their legal rights. The test, as applied in *Re Pauling's ST* [1964] Ch 303 (CA), is whether it would be just to allow the beneficiary to 'turn round and sue the trustees' over actions in which the beneficiary participated or to which the beneficiary consented.

Of course, a beneficiary who is not *sui juris* cannot consent, and a beneficiary who is *sui juris* must consent for themself. If an individual beneficiary consents to the trustees departing from the trust, they are not able to sue for breach, but the other beneficiaries can. Where a beneficiary consents to a breach causing loss to the trust fund, their interest under the trust may be 'impounded', in particular circumstances (*Chillingworth v Chambers* [1896] 1 Ch 685; Trustee Act 1925, s.62) that is to say, as much of the value of their interest as is needed will go to making up the loss to the trust fund.

16.3.3 Trustee exemption clauses

A trust instrument may contain a clause which exempts trustees from personal liability for breach of trust. There is no exemption from proprietary liability, for if the trustee is holding a trust right or its traceable proceeds in their hands, equity will simply require them to hold that asset or proceeds on trust. The clauses, if effective, will exempt the trustees from personal liability to restore a trust with money taken from their own pockets.

The principles defining the valid scope of trustee exemption clauses were the subject of discussion by Millett LJ in *Armitage v Nurse* [1997] EWCA Civ 1279, [1998] Ch 241. He said that the trustee's duty to act loyally, honestly, and in good faith were an 'irreducible core' set of trust obligations, breach of which could not be relieved by any exemption clause. A trustee exemption clause can validly relieve a trustee of liability for a breach evincing any other kind or degree of fault. No matter how grossly negligent a breach may be, a properly drawn clause can relieve a trustee of liability for the consequent loss. According to Millett LJ, a trustee may even be relieved of liability for an intentional breach of trust if it was undertaken with the best interests of the beneficiaries in mind. This last point was doubted in *Walker v Stones* [2001] QB 902 (CA). Perhaps a clause should relieve a trustee of a 'one-off' breach of this kind, but a consistent intentional disregard of the trust terms should not be relieved, even if the trustee does so honestly, for this would allow the trustee to rewrite the trust. If that is desirable, the proper procedures for varying the trust should be followed (Chapter 15). Reckless breaches (i.e. where the trustee knowingly takes risks with the beneficiaries' interests) count as dishonest or disloyal breaches, and cannot be relieved, and this includes the case where the trustee undertakes a breach advertently relying on the exemption clause to get himself off the hook if things go wrong.

*Armitage v Nurse* is a controversial decision. In response, the Law Commission published a consultation paper (No. 171, 2003) proposing that any exemption clause purporting to relieve a trustee of liability for negligence or worse (i.e. recklessness, dishonesty, and so on) would be invalid at law. However, after consultation, they decided to recommend no legislative change, and leave the various professional regulatory bodies to ensure that settlors were informed of the effects of trustee exemption clauses by those offering the services of trustees (Law Com 301, 2006).

16.3.4 Section 61 Trustee Act 1925

Section 61 empowers the court to relieve a trustee of all or part of their liability for breach of trust if they have 'acted honestly and reasonably, and ought fairly to be excused for the breach of trust'. Each limb of the test (honesty, reasonableness, and fairness) must be met. There is little case law on the application of the section. Relief
was denied where the trustee’s breach manifested a conflict of interest (Re Pauling’s ST) and also in Barlett v Barclays Bank Trust Co Ltd [1980] 1 Ch 515, where a professional trustee made a risky unauthorised investment, on the ground that the breach was unreasonable and that the trustee ought not fairly to be excused at the beneficiaries’ expense. The section was successfully pleaded in Evans v Westcombe [1999] 2 All ER 777 to partly relieve a lay administrator of an estate who distributed rights in the reasonable belief that one beneficiary of the estate, who later turned up, had died.

SELF-ASSESSMENT QUESTIONS

1. In what circumstances will trustees all be liable together?
2. In what circumstances will a trustee not be liable for a breach of trust?
3. When can a trustee claim an indemnity from co-trustees?
4. What is necessary for a beneficiary’s consent to a departure from the trust terms to be valid?
5. What does it mean for a beneficiary’s interest to be impounded?
6. To what limits may a trustee exemption clause go to relieve a trustee of liability for breach of trust?
7. In what circumstances will the court relieve a trustee under s.61 of the Trustee Act 1925?

Summary

Where a trust is breached, a trustee may be either (a) personally liable to carry out the trust or pay for a loss out of their own pocket, or (b) proprietarily liable to hold rights (or their traceable proceeds) the trustee has misappropriated on trust for the beneficiaries. Claims for breach of trust are traditionally framed in terms of ‘falsifying’ the trust account, where a particular transaction is identified as a breach of trust or ‘surcharging’ the trust account, where a general or particular failing on the part of the trustee means that the value of the trust rights is lower that it should be. The rules for assessing personal liability for causing losses in these cases differ from each other and both are traditionally regarded as different from the common law rules governing causation of loss. Trustees may all be liable where they acted (or should have acted) together in circumstances where a breach has occurred, but are solely liable for their own individual breaches committed without the participation of other trustees. Sui juris beneficiaries can consent to departures from the trust terms, but a trustee breaches a trust in respect of any departures as regards those beneficiaries who cannot or do not consent. A beneficiary who consents to a breach may have their interest impounded to make up the loss to the trust occasioned by the breach. Trustees may be relieved of liability under the trust instrument by an exemption clause, which is valid even if very widely drawn, but dishonest or reckless breaches may not be relieved. Section 61(1) of the Trustee Act 1925 empowers the court to relieve a trustee of all or part of the liability for an honest and reasonable breach.

16.4 Liability of third parties

So far, we have outlined the liability of a trustee for breach of trust. However, beneficiaries may also have very important remedies against various third parties (i.e. not the trustee) who are somehow involved in a breach of trust.

The most straightforward case of third party liability for breach of trust arises when a person, though not formally appointed, takes it upon himself to act as a trustee. Such a person, called a trustee de son tort (a trustee by their own wrong), is liable for any breach of trust they commit just as would be a properly appointed trustee (see Mara v Browne [1896] 1 Ch 199). The term ‘constructive trusteeship’ properly applies in this context because a person is by operation of law held to be a trustee (see below, Sections 16.5 and 16.6).
Proprietary liability of third parties

More typically, it is other third parties who are sought to be made liable. In the first place, if the trustees transfer trust rights in breach of trust to a someone who is not a bona fide purchaser (recall Section 4.1.1), the beneficiaries may simply call on that person to return the rights, or their traceable proceeds. We can refer to this liability as the proprietary liability of third parties, for the beneficiaries enforce their rights to specific assets held by third parties. Although, as we will see in Chapter 19, the rules governing tracing are complicated, this liability is essentially straightforward. Where the beneficiaries can identify an asset that was previously held on trust, or its traceable substitute, in the hands of a third party, they can claim it as theirs in equity. The court will require the third party to transfer the right to the beneficiaries in certain cases, but more usually to their trustees (usually new trustees will replace the old ones who committed the breach in the first place).

Personal liability of third parties

Secondly, however, third parties will sometimes be personally liable (i.e. liable to pay money from their own pockets) to make up the loss to the trust fund caused by a breach of trust. They will be required to do so in two cases:

1. where they have dishonestly assisted in the breach of trust by the trustee and
2. in certain cases where they have received trust rights dissipated in breach of trust.

We will now look at the personal liability of third parties in detail.

16.5 Dishonest assistance (accessory liability)

A third party (i.e. someone who is neither a trustee nor beneficiary) may participate or assist in a breach of trust. A typical accessory to a breach of trust might be a solicitor who normally works with the trustees to carry out the terms of the trust, but who becomes involved in assisting them in a transaction which breaches the terms of the trust. Traditionally, such a person could be held liable for ‘knowing assistance’ in a breach of trust. The term ‘knowing’ indicates that some sort of knowledge of involvement in a breach of trust was required before the third party could be held liable. Because the liability was to restore the trust out of their own pocket, it was said that the assistant was liable as a ‘constructive trustee’, meaning that they were personally liable for the same amount ‘as if they were a trustee’. This terminology of ‘constructive trusteeship’ is now generally frowned upon because of its potential for confusion. People may be called ‘constructive trustees’ either because they are being treated like trustees even though they are not or because they are actual trustees of constructive trusts. It is very important to distinguish between the two.

The leading cases on accessory liability are the decisions of the Privy Council in Royal Brunei Airlines Sdn Bhd v Tan [1995] UKPC 4, [1995] 2 AC 378, and Barlow Clowes International Ltd v Eurotrust International Ltd [2005] UKPC 37, [2006] 1 All ER 333, [2006] 1 WLR 1476, and the decision of the House of Lords in Twinsectra Ltd v Yardley [2002] UKHL 12, [2002] 2 AC 164. They established that an accessory must dishonestly assist a breach of trust in order to be liable. Mere negligence was insufficient to found liability. It does not matter whether the trustee himself was fraudulent or dishonest in committing the breach. A solicitor who dishonestly advised an innocent trustee to commit a breach would be liable all the same. All turned on the accessory’s dishonesty.

What then counts as dishonesty? Briefly, the Privy Council in Royal Brunei advised that while dishonesty requires that the accessory know the facts which to a reasonable person would indicate that they were participating in a breach of trust, and so in that sense is subjective, the test for honesty is objective in that the standard of honesty is determined by the views of honest and reasonable people. The accessory is not allowed to set their own standard of honesty, such that if they personally see nothing wrong with breaching a trust they could claim to be honest. In Twinsectra, the House of Lords either refined or confused the Royal Brunei test for dishonesty (depending
on your point of view) holding that though the test of morality was an objective one, it had to be shown that the defendant subjectively knew that his conduct fell below that objective standard. That third requirement was shortly afterwards removed by the Privy Council in Barlow Clowes v Eurotrust Ltd. The question then is what an English court, bound by Twinsectra but not Barlow Clowes, is to do. The Court of Appeal decided that they should follow the latter: Abou-Rahmah v Abacha [2006] EWCA Civ 1492, [2007] Bus LR 220.

**Activity 16.5**


There are two issues in the case, one concerning the requirements for accessory liability, the other concerning the nature of Quistclose trusts. Concentrate for the moment only on those passages dealing with accessory liability.

Explain the ‘combined test’ for dishonesty stated by Lord Hutton and preferred by the majority of the House, and the ‘objective test’ of Lord Millett in dissent.

Would we be better to return to the nomenclature of ‘knowing’ rather than ‘dishonest’ assistance?

**16.6 Recipient liability**

One must be very careful here. We have already mentioned (Section 16.4) the proprietary liability of third parties who hold trust assets or their traceable proceeds in trust (discussed further in Chapter 19). What we will look at now is the personal liability of third parties for having received or dealt with trust assets or their traceable proceeds which they received in breach of trust. Consider the following breaches of trust. Tom, the trustee, in breach of trust withdraws money from the trust’s bank account to give £1,000 to each of his children, Martha and Graham, as birthday presents. Martha spends her £1,000 on a holiday. Graham spends his on a scooter. The beneficiaries have a proprietary claim against Graham, for he retains the traceable proceeds (his title to the scooter) of the £1,000 trust money he received. They can go to Graham, point to the scooter, and say, ‘you hold it on trust for us’. A court will require Graham to transfer it to them or to the new trustees (supposing, as is likely, that Tom has been replaced).

What can they say to Martha? She has nothing left of what she received, for she spent it in a way which gives rise to no traceable substitute. What we are looking at now is whether the beneficiaries can require Martha to dig into her own pocket and pay £1,000 to each of his children, Martha and Graham, as birthday presents. Martha spends her £1,000 on a holiday. Graham spends his on a scooter. The beneficiaries have a proprietary claim against Graham, for he retains the traceable proceeds (his title to the scooter) of the £1,000 trust money he received. They can go to Graham, point to the scooter, and say, ‘you hold it on trust for us’. A court will require Graham to transfer it to them or to the new trustees (supposing, as is likely, that Tom has been replaced).

What can they say to Martha? She has nothing left of what she received, for she spent it in a way which gives rise to no traceable substitute. What we are looking at now is whether the beneficiaries can require Martha to dig into her own pocket and pay £1,000 to restore the value of the trust fund. In other words, we must consider whether Martha is personally liable to restore to the trust the value received. Traditionally, Martha would only be liable to do so if she had some degree of knowledge that she received the £1,000 in breach of trust (hence the fact that this species of liability is sometimes termed ‘knowing receipt’), or following receipt she acquired some degree of knowledge that the rights were trust rights and then dealt with them as her own anyway instead of returning them to the trust (hence the term, ‘knowing dealing’). As in the case of ‘knowing assistance’, because her personal liability to restore the trust was of the same kind as the breaching trustee, she was typically called a ‘constructive trustee’, because she was liable to restore the loss caused to the trust ‘as if’ she were a trustee.

**16.6.1 The standard of knowledge required**

Fixing on a standard of knowledge for the personal liability of a recipient of trust rights has exercised the brains of many judges in many cases. The issues were complicated by the fact that, because knowing assistants and knowing recipients were traditionally both treated as ‘constructive’ trustees (i.e. as if they were trustees), it was often felt that the standard of knowledge for liability in both cases was the same. In Royal Brunei, the Privy Council firmly distinguished the two heads of liability, saying that there was no reason why the standards should be the same, and this principle was enthusiastically accepted (albeit obiter) by the House of Lords
in Twinsectra. Determining the standard was also complicated by the distinction between knowledge and notice. You will recall (Section 4.1.1) that a standard of ‘notice’ is used to assess whether a recipient of trust party is a bona fide purchaser. Notice generally applies in circumstances, such as a conveyance of a title to land, in which the purchaser should protect themselves by investigating in a reasonably diligent fashion the title they intend to buy in order to be free of any competing rights to it. In typical cases of breach of trust, however, the recipients have no reason to investigate the source of the rights they receive. In our examples, Graham and Martha do not ask their father, Tom, to prove that the money they receive is his to give, nor would they be expected to do so. Thinking in terms of notice, which some judges appeared to have done, muddies the waters.

Re Montagu’s Settlement Trusts

Prior to the Court of Appeal decision in Bank of Credit and Commerce International (Overseas) Ltd v Akindele [2000] EWCA Civ 502, [2001] Ch 437, the leading case (amongst many others) was probably Re Montagu’s ST [1987] Ch 264. In Montagu the trustees gave the defendant a number of paintings held under a family settlement. This was a breach of trust. The defendant at one time knew that the paintings were part of the family settlement, but had forgotten that fact and treated them as his own. He sold the paintings, and after his death many years later (when there was no longer any possibility of tracing the proceeds of the sale), his son, as the principal beneficiary of the family settlement, claimed that the defendant’s estate was liable to restore the value that had been lost. Megarry J denied the claim. He held that in order to found a claim for knowing receipt or dealing, the defendant had to have actual knowledge that his receipt was in breach of trust, was ‘wilfully blind’ to that fact (i.e. had shut his eyes to the obvious) or had wilfully and recklessly failed to make the inquiries that an honest and reasonable person would make. Furthermore, a person was not liable for knowledge they might have once had, but had honestly and genuinely forgotten when the breach occurred.

BCCI v Akindele

In Akindele, the defendant entered into an arrangement with the plaintiff bank to buy shares. The contract was an unusual one, in that the ‘share purchase’ was basically a sham. The real contract was to provide a loan to the bank for a certain time period in return for which the bank guaranteed a repayment of the loan at a high rate of interest. The actual transaction was entered into on behalf of the bank by several of its employees as part of a fraud on the bank. The claimant bank sued the defendant for the large amount of interest he received under the transaction, claiming that the sham nature of the transaction and the high rate of interest would have indicated to a reasonable and honest person that the transaction was fraudulent, or at least have caused a reasonable or honest person to make further inquiries before entering into the transaction. The claimant bank’s claim failed. In essence, the court accepted the defendant’s explanation that he believed the transaction and the high rate of interest under it were legitimate investments offered to him as one of the bank’s ‘high net worth’ clients. He did not concern himself with the details of the contract, and so did not regard the odd aspects of the transaction to be a matter of concern. Nevertheless, the case was not decided on the terms of the law as stated in Re Montagu. Nourse LJ decided that just as Royal Brunei had cleared away the tangled case law of the past to establish from first principles the basis upon which a person could be liable for assisting a breach of trust, the court should do the same for the law on recipient liability. He said that a defendant would be personally liable only if it would be ‘unconscionable’ for him to retain the benefit of the receipt of trust property. Ironically, this is the one word which was rejected by the Privy Council in Royal Brunei as devoid of meaning and therefore completely unworkable. It will come as no surprise to learn that Nourse LJ did not provide any clear guidance about the factors which would go to make the retention of benefit unconscionable, and the law is now more uncertain than ever. This is an area of the law that calls for an extensive review and reasoned decision by the Supreme Court.
It is to be noted that in *Re Montagu* the recipient was a volunteer (i.e. a donee who gave no consideration for the transfers) and so could not claim to be a *bona fide* purchaser. However, if the paintings had still been in his possession (or in his estate), they would have belonged in equity to the beneficiaries. In short, there was no proprietary liability because the paintings had been sold long ago and the proceeds dissipated so as to be untraceable. In *Akindele*, by contrast, the defendant had given consideration under a valid contract for the assets he received (he had given the bank the use of his money for two years under a contract). In *Re Montagu*, the recipient got to keep the value of property he received and had not paid for in any way, whereas in *Akindele*, if he had been liable, he would have lost value for which he had paid. Given the differences in these two situations, should the standard of knowledge be lower in the case of a donee recipient? Should it be ‘unconscionable’ for a donee ever to retain the benefit of their receipt, being one who, to repeat, paid nothing for what they received in breach of trust?

Charles Mitchell and Stephen Watterson have argued convincingly that liability of knowing receipt is actually liability for breach of trust, which arises when the recipient dissipates the trust assets with knowledge of the existence of the bare trust (to restore the trust assets to the proper trustees) which arose when the assets were received: ‘Remedies for knowing receipt’ in Mitchell, C. (ed) 2010, p.115.

There is also a strong argument that cases like *Akindele* really have nothing to do with knowing receipt. *Akindele* concerned a breach of fiduciary duties by company directors. There was no breach of trust. The directors acted as agents for the company to make a contract with the defendant. Clearly, they did not have actual authority to commit a fraud on the company, so the essential question was whether the defendant relied on their ostensible (i.e. apparent) authority to make the contract. He did and so the contract was binding. If not, the contract would have been void and the money recoverable at common law. Knowing receipt was irrelevant. See R. Stevens ‘The proper scope of knowing receipt’ [2004] 4 LMCLQ 421; Criterion Properties plc v Stratford UK Properties LLC [2004] UKHL 28, [2004] 1 WLR 1846. Perhaps the main difficulty in this area of law is that most of the modern cases of knowing receipt are company law cases. *Re Montagu* stands out because it is a case dealing with breach of trust.

### 16.6.2 An unjust enrichment approach

The Court of Appeal in *Akindele* briefly referred to a new approach to the personal liability of a recipient, an unjust enrichment approach. The court felt itself bound to work within the constraints of previous case law and unable to consider this approach, but as it has been mooted extra-judicially by some of the most senior members of the bench (Lord Nicholls, whose views are quoted in *Akindele* on this issue, and Lord Millett), and since this area of law is ripe for review by the Supreme Court, it should be considered. From an unjust enrichment perspective, the recipient of rights transferred in breach of trust should be strictly liable to repay its value to the trust, for otherwise they would be unjustly enriched at the expense of the beneficiaries. Their liability should not turn on their knowledge, but purely on the fact that they were enriched, at the beneficiaries’ expense, in circumstances where they ought never to have received that enrichment. In these terms, the case is similar to if you paid your gas bill a second time by mistake, forgetting that you had already sent a cheque. The gas company is strictly liable to return the second payment because they would otherwise be unjustly enriched at your expense. Your mistake means that your intention to enrich the company was vitiated and so should not count against you. The same goes, on this reasoning, for the recipient of trust rights dissipated in breach of trust. The beneficiaries give no consent whatsoever to the transfer, so the case is even stronger than mistake.

**The ‘change of position’ defence**

The strict liability of the unjust enrichment defendant is modulated by the defences of *bona fide* purchase and change of position. Innocent recipients who give value in return will normally be fully protected as *bona fide* purchasers. The change of position...
defence can protect innocent donees who rely upon the apparent security of the receipt without knowledge of the breach of trust. It can apply if they use the value received in a way which they would not have done but for having received them. By doing so, they change their position so that it would be unjust to make them pay it all back, and to that extent, they can be relieved of liability.

The defence is best explained by an example. Consider Martha, above, who spent her birthday gift on a holiday. Assume she was innocent of the fact that Tom gave her the money in breach of trust. If she can show that she would not have gone on holiday but for the £1,000 gift, and that she went only because the £1,000 gift made her rich enough to afford it, then she can claim that her position has changed. She innocently spent money in a way she would not have done out of her own pocket given her previous finances, and it would be unjust now to make her pay it back because that would put her in a worse position than if she had never received the money at all.

Unlike _bona fide_ purchase, which is an ‘all or nothing’ defence, change of position can be a partial defence, reducing liability only to the extent that the defendant has changed their position. So, for example, if Martha had spent only £600 on the holiday in reliance on her receipt of the £1,000, she might have her liability in unjust enrichment reduced to £400.

It is important to note that while the unjust enrichment approach has both academic and practitioner supporters, there is no case which adopts this approach to recipient liability. Until such time, this approach to the personal liability of the recipient must be speculative.

**Activity 16.6**

Ted is the trustee of the Davis family trust. He takes home two paintings which are held on the family trust, puts one on his wall and he sells the other for £2,000. Ted then makes an unauthorised investment which causes a loss to the trust of £20,000. Alex, his solicitor, who advised him on the investment, read the trust terms incorrectly and concluded the investment was authorised. Ted then decided to transfer £50,000 to Barbara, a non-beneficiary; Alex carried out the transaction. Ted gives the trust painting on his wall to Fred, another non-beneficiary, who sells it for £10,000 and spends the money on a lavish birthday party for his wife.

List the possible proprietary and personal claims the beneficiaries have against (a) Ted, (b) Alex, (c) Barbara, and (d) Fred in the following situation, and state what the appropriate test for liability is in each case.

**Essential Reading**

At least one of the following:

- Pettit, Chapter 8: ‘Constructive trusts’; Chapter 23: ‘Breach of trust’.

**Further reading**


ACTIVITY 16.7
Read Re Montagu’s ST and BCCI v Akindele.

Which approach to personal recipient liability is more persuasive? Does the unjust enrichment approach seem preferable to both?

SELF-ASSESSMENT QUESTIONS
1. Who or what is a trustee de son tort?
2. What is ‘knowing dealing’?
3. What is ‘accessory liability’?
4. What are the essential duties of trustees, according to Millett LJ in Armitage v Nurse?
5. Why is the decision in Armitage v Nurse considered controversial?
6. What is ‘falsifying the trust account’?
7. What is liability for ‘equitable compensation’? How does it differ from a trustee’s ‘liability to account’?

Summary
A third party may participate in a breach of trust. Traditionally, they would be personally liable for ‘knowing assistance’. This liability would be one to restore the trust from their own pocket. To be liable, the third party must ‘dishonestly assist’ the breach of trust. Mere negligence is not enough. The test for dishonesty has now arguably returned to one of knowledge.

If a third party receives assets dissipated in breach of trust and they are retained or substituted for other assets, the beneficiaries can force the third party to hand them back to the trust. However, if the assets are dissipated and there is no exchange product, the extent of the third party’s degree of knowledge determines whether they will be personally liable to restore their value. The standard of knowledge required has been debated over the years in many judicial decisions.

The standard of knowledge may differ between ‘knowing assistance’ and ‘knowing receipt’. The law is currently unclear. However, according to Re Montagu, it would appear that to fix a recipient donee with liability, the defendant would be required to have ‘actual knowledge’ that the receipt was in breach of trust, was ’wilfully blind’ to the obvious, or failed to make inquiries that an honest and reasonable man should make. According to Akindele, fixing a recipient with liability who has given consideration for the receipt is only possible where it would be ‘unconscionable’ for the defendant to retain the benefit of the receipt of the trust property.
An unjust enrichment approach to recipient liability has recently been proposed, though no case has actually adopted it. On this approach, a recipient of rights dissipated in breach of trust should be strictly personally liable to repay its value to the trust, for otherwise they would be unjustly enriched at the expense of the beneficiaries. However, this liability is subject to the defences of bona fide purchase and change of position. If an innocent recipient relies upon the legitimacy of the receipt and uses the rights in a way which they would not have done had they not received them, and in doing so ‘changes his position’ making it unfair for them to pay all or some of it back, their liability will be reduced accordingly.

**SAMPLE EXAMINATION QUESTIONS**

**Question 1** To what extent is a third-party defendant’s state of knowledge relevant in claims for personal liability to restore the trust?

**Question 2** Stanley was a solicitor who often advised Tom, the chief trust officer of a large trust company. In 2004, he advised him to invest a large portion of the value of the Adams family trusts in investments prohibited by the trust instrument to enhance the returns on the trust fund. Tom agreed with the idea, and did so. The strategy was unsuccessful and the trust fund is now worth only half of what it was. In 2005, Stanley negligently prepared a tax-saving scheme for the Bryson family trust, which Tom implemented, and which resulted in an unnecessary £30,000 tax liability. In 2006, Tom asked Stanley to prepare the documentation for the transfer of a house from the Carling family trust to the widow of the family. Stanley was sceptical about whether the transfer was permitted by the terms of the trust, but in response to his query on this point, Tom said, ‘I think it’s okay, and the widow needs the house, and in any event I’m covered by the exemption clause. Get to it.’ Stanley carried out the transfer as instructed. All three trust instruments contain exemption clauses relieving trustees of liability for any loss to the trust except when caused ‘by his own actual fraud’. Advise the beneficiaries of each of the trusts.

**Question 3** Tamara, a trustee, breaches the trust she manages by (1) failing to invest the trust rights with due care so that the fund is worth much less than it should be; (2) by selling a title to a parcel of land held by the trust, a transaction prohibited by the trust terms; (3) by making an unauthorised payment to Barney, one of the beneficiaries who realises it is a breach of trust but consents to it.

Advise Tamara.

**ADVICE ON ANSWERING THE QUESTIONS**

**Question 1** The question concerns personal liability both for ‘intermeddling with’ the trust rights so as to become a *trustee de son tort*, assistance in a breach of trust, and for receipt of trust rights dissipated in breach of trust. Regarding the first, knowledge is in a certain sense irrelevant, for the *trustee de son tort* by their actions makes plain that they are acting as if they were a trustee of the trust. One cannot do that unknowingly, though whether the intermeddler realises their potential liability is irrelevant. As to assistance, the question requires an analysis of the test of dishonesty now set in place by the Privy Council in *Barlow Clowes*, purporting to follow the majority in *Twinsectra*, themselves purporting to follow *Royal Brunei Airlines*. Finally, recipient liability must be discussed, first examining the law defining the standard of knowledge for knowing receipt prior to *Akindele*, and then considering how knowledge might figure in the *Akindele* ‘unconscionability’ test. The unjust enrichment approach should be considered as a possible way forward regarding recipient liability, and it should be pointed out that on this approach the issue of the defendant’s knowledge comes into play only when the change of position defence is invoked.

**Question 2** The investment is clearly in breach of trust. The account can be falsified against Tom in respect of this transaction. The issues are whether Tom can be relieved by the exemption clause, and whether Stanley may be liable as an accessory. As to the former, Millett LJ in *Armitage* stated that an intentional breach carried out honestly for the benefit of the beneficiaries would not count as wilful fraud. As for Stanley, he is not protected by the exemption clause, and having intentionally breached the trust, he may be regarded as dishonest, although Millett LJ’s reasoning regarding the
trustee might by analogy be applied to Stanley, so that he could not be treated as dishonest under the test laid down in \textit{Royal Brunei}, \textit{Twinsectra} or \textit{Barlow Clowes}. The test should be discussed in detail and applied as well as it can be to Stanley. Tom is not liable for the loss caused by the negligently prepared tax-saving scheme unless he was negligent in his appointment or monitoring of Stanley, and there is no evidence of this. Stanley is liable for his professional negligence. Tom, on behalf of the trust, should pursue a claim for damages for professional negligence against Stanley. The trust account can clearly be falsified in respect of the final transaction. Tom will be personally liable unless relieved by the exemption clause, but this is doubtful, for as Millett LJ said in \textit{Armitage}, a trustee who intentionally relies on an exemption clause to carry out a possible breach of trust is wilfully reckless and thus dishonest, so the exemption clause will not operate in their favour. Stanley may be liable here for assistance, depending upon whether you would characterise his state of mind as sufficiently dishonest under the test in \textit{Royal Brunei}, \textit{Twinsectra} or \textit{Barlow Clowes} (i.e. did he act in a wilfully blind fashion, failing to make enquiries?). The widow will be subject to a proprietary claim for the title to the house. As a donee, she is not a \textit{bona fide} purchaser. If she has managed to dispose of the title, the beneficiaries can trace into the proceeds. If those have been dissipated, the widow may be subject to a personal claim, in respect of which a discussion of \textit{Montagu}, \textit{Akindele} and unjust enrichment is required.

\textbf{Question 3} Tamara must be advised that she will be personally liable for each of the three breaches of trust. Regarding (1), the beneficiaries can surcharge the account, and the amount of compensation she will have to pay to restore the trust will be such as to place the trust in the position it would have been in had she invested with care. The rules of causation in this respect are likely to be analogous to those of the common law (Millett LJ in \textit{Mothew}), though the rule from \textit{Target Holdings} is the ‘common sense causation with the full benefit of hindsight’ test. In Nestle \textit{v} National Westminster Bank (recall Chapter 4, Activity 4.7), the court held that if the trustee had been liable, compensation would have been awarded to bring the fund up to the level it would have had, had a proper investment policy been followed, not merely the minimum level the trustee might have achieved without being subject to a legal challenge. Regarding (2), the sale can be falsified on the trust account. Tamara should, if she can, restore the trust by re-purchasing the title to land for it. If she cannot, the compensation she will pay will be determined as the value of the title at the time of trial (\textit{Nocton v Lord Ashburton}; \textit{Target Holdings}) minus, of course, the amount received by the trustees in payment for it. Regarding (3), Tamara will again be liable to restore the trust for the loss caused by this falsifiable appointment. She may, however, be relieved in whole or in part as Barney’s interest may be impounded (\textit{Chillingworth v Chambers}; Trustee Act 1925, s.62). Tamara should also be advised that the beneficiaries may well apply to the court to have her replaced.
**Reflect and review**

Look through the points listed below.

Are you ready to move on to the next chapter?

**Ready to move on** = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

**Need to revise first** = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

**Need to study again** = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>I can describe the various ways in which a trust can be breached.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain the various personal and proprietary rights that the beneficiaries may have against trustees and third parties when a trust is breached.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain how the beneficiaries may claim that a trustee has breached the trust by ‘surcharging’ or ‘falsifying’ the trust accounts.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain the liability of trustees for breach of trust between themselves, and the consequences of a beneficiary’s consent to a breach of trust.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain and apply s.61 of the Trustee Act 1925 and the law governing trustee exemption clauses.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain and apply the tests which govern third party liability for assisting in a breach of trust and receiving trust property.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>16.1 Liability of a trustee for breach of trust</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>16.2 Personal liability of a trustee for breach of trust</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>16.3 Liability of trustees <em>inter se</em></th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>16.4 Liability of third parties</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>16.5 ‘Dishonest assistance’ or ‘accessory liability’</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>16.6 ‘Recipient liability’</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>17.1</td>
<td>Fiduciary obligations and 'conflict of interests'</td>
<td>189</td>
</tr>
<tr>
<td>17.2</td>
<td>The 'no conflict' rule</td>
<td>190</td>
</tr>
<tr>
<td>17.3</td>
<td>The 'no unauthorised profits' rule</td>
<td>191</td>
</tr>
<tr>
<td>17.4</td>
<td>The 'self-dealing' rule</td>
<td>191</td>
</tr>
<tr>
<td>17.5</td>
<td>The 'fair-dealing' rule</td>
<td>192</td>
</tr>
<tr>
<td>17.6</td>
<td>Equitable compensation for breach of fiduciary obligation</td>
<td>193</td>
</tr>
<tr>
<td>17.7</td>
<td>The uncertain application of trustee exemption clauses</td>
<td>194</td>
</tr>
</tbody>
</table>

Reflect and review ................................. 197
Introduction

Fiduciary obligations are particular (and peculiar) obligations recognised by equity. In certain circumstances, typically in trusts but also in agency and other relationships, equity will require one party to the relationship, called the 'fiduciary', to act in the best interests of the other, called the 'principal'. Failure to do so will mean that the fiduciary commits the equitable wrong of breach of fiduciary duty vis-à-vis the principal. Most trustees are fiduciaries who must act in the best interests of their principals, the beneficiaries. The contours of the fiduciary obligation are very much revealed by the circumstances in which the fiduciary is held to have breached the obligation by not acting with their principal's best interest in mind, and so we will go through the various cases of breach of fiduciary obligation in turn.

Essential reading

- Chapter 4 of this subject guide, Section 4.2.
- Penner, Chapter 2: 'Property, obligations, and trusts', paras 2.10–2.16, 2.25.
- Penner, Chapter 12: 'The law governing fiduciaries'.

Learning outcomes

By the end of this chapter and the relevant readings you should be able to:

- explain what fiduciary obligations are, and distinguish them from other obligations a trustee might have
- describe the consequences which attach to the receipt by a fiduciary of an unauthorised profit
- explain what happens when a trustee purchases trust rights or sells rights to the trust
- describe the circumstances in which a trustee may safely purchase the interest of a beneficiary
- explain and apply the law governing equitable compensation for breach of fiduciary obligation
- explain the uncertainty regarding the application of trustee exemption clauses to a breach of a trustee's fiduciary obligation.
17.1 Fiduciary obligations and ‘conflict of interests’

17.1.1 Fiduciary relationships

The nature of the fiduciary obligation has been the subject of much discussion and controversy. It has been traditionally characterised as comprising duties of loyalty, altruism, and disinterestedness. Roughly, the idea is that fiduciaries must place the interests of their principals above all other considerations when they act to affect the interests of their principal. While trustees typically owe fiduciary duties to their beneficiaries, there are a range of other fiduciary relationships, such as agent and principal, director and company, solicitor and client and among business partners.

The essence of a fiduciary relationship is that the fiduciary is in a position to exercise discretion in carrying out the duties for their principal. So, for example:

- a trustee has discretion in investing the trust rights
- an agent has discretion in making contracts for the principal
- company directors exercise discretion in the way they run the company, for example, in hiring a chief executive.

In exercising these discretions, fiduciaries must think only of the best interests of their principals and not be swayed by their own interests or the interests of any third parties. They are therefore prohibited from exercising their discretions in ways that manifest conflicts of interests. So a trustee should not invest the trust rights in her own company because her company needs capital. An agent should not enter into a contract of employment on behalf of her principal with her brother-in-law because he needs a job. A company director should not buy raw materials for the company from their own business. The basic rule governing fiduciary obligations is the ‘no conflict’ rule. Fiduciaries must not place themselves in situations where their own interests (or duties to others) conflict with the interests of their principals.

17.1.2 Breaches of fiduciary duties

It has been argued that any breach by a trustee of their duties under a trust is a breach of fiduciary duty (P. Birks ‘The content of fiduciary obligations’ (2002) 16 Trust Law International 34). Not all would agree with this. Thus, the Court of Appeal held that a trustee’s breach of a duty of care and skill is not a breach of fiduciary obligation (Bristol & West Building Society v Mothew [1988] Ch 1), nor is the standard case of breach of trust where a trustee makes an unauthorised investment or pays a non-beneficiary, unless the trustee does so because of a conflict of interest. In the same way, an agent who breaches their contract of agency is not at the same time always in breach of their fiduciary duty. A breach of fiduciary duty, it has been said, generally only occurs when the fiduciary does something they are entitled to do, but in a way that shows that they are not acting with the principal’s best interests in mind.

So, for example, a trustee is entitled to enter into authorised investments. If the trustee enters into an unauthorised investment, they breach the trust but this is not necessarily a breach of the trustee’s fiduciary duty. Consider instead an investment which is within the terms of the trust, such as shares in a mining company. Normally they would be perfectly entitled to make the investment, but if they sold their own shares in the mining company to the trust, then this otherwise valid investment would reveal a clear conflict of interest.

Activity 17.1

Why specifically is there a conflict of interest in the above example?

By investing in this way the trustee does not breach the trust terms on investment, but breaches the fiduciary obligation owed to the beneficiaries.
Summary

A fiduciary obligation is traditionally seen as a duty of loyalty and good faith. The fiduciary must place the interest of the principal above all other considerations. Fiduciary obligations can occur in a range of relationships. A fiduciary is in a position to exercise discretion in carrying out their duties and consequently in performing these duties, the fiduciaries must think only of their principal's best interests and not of their own or those of third parties. This is known as the 'no conflict rule', a fiduciary must not place themselves in a position of conflict of interest or duty.

A breach of fiduciary duty generally occurs when a fiduciary does something they are entitled to do, but in such a way that they are not acting with the principal's best interests in mind. Consequently, not all breaches of trust are a breach of fiduciary duty. For example, the breach of care and skill in making trust investments, although unfortunate, is not a breach of a fiduciary obligation. Some, such as Birks, argue to the contrary.

17.2 The ‘no conflict’ rule

This is the general rule governing the behaviour of fiduciaries: a fiduciary must not place herself in a position where her own interests (or duties to others) may come into conflict with the interests of her principal. In other words, a fiduciary must not allow her duty to her principal to come into conflict with her own interests or other duties.

The leading case is *Boardman v Phipps* [1966] UKHL 2, [1967] 2 AC 46.

Activity 17.2

Read *Boardman v Phipps* and:

a. explain the views of the majority and the minority in the case;

b. state which view(s) you prefer, giving your reasons.

You should take care to note that a fiduciary can breach their fiduciary obligations entirely honestly, as in *Boardman*. Although traditionally a breach of fiduciary obligation was sometimes called equitable fraud or constructive fraud (see *Nocton v Lord Ashburton* [1914] AC 932; *Armitage v Nurse* [1997] EWCA Civ 1279, [1998] Ch 241), no fraudulent intentions are required. The breach does not turn on the fiduciary's state of mind (i.e. whether or not the fiduciary realises they are acting in a situation of conflict) but on whether there is in fact a conflict of interest.

*Boardman* was a case which involved a trust, but most of the situations in which the 'no conflict' rule has been applied concern company directors and agents (*Regal (Hastings) Ltd v Gulliver* [1942] UKHL 1, [1942] 2 AC 134; *Industrial Development Consultants Ltd v Cooley* [1972] All ER 162, [1972] 1 WLR 443). Because these fiduciary obligations arise in commercial circumstances, it has been argued that the 'no conflict' rule must be applied realistically and contextually. For conflicts of interest in such situations are endemic, and typically the subject of contractual negotiation between fiduciaries and their principals. For example, contractual provisions may allow company directors to determine their own levels of pay or whether a director of a company may hold another directorship with a competing company.

Unless the principal consents, a fiduciary may not operate a competing business (*Re Thomson* [1930] 1 Ch 203), but the scope of that prohibition is not entirely clear. It has been said that a stringent application of the rule to business opportunities may be economically inefficient, reducing incentives to generate wealth, and anti-competitive in certain circumstances. (See *Peso Silver Mines Ltd v Crapper* [1966] SCR 673, 58 DLR (2d) 1 (Canada); *Canadian Aero Services Ltd v O'Malley* [1974] SCR 592, 40 DLR (3d) 371 (Canada); *Guth v Loft Inc* [1939] 5 A 2d 503 (Delaware); *Braz v Cellular Information Systems Inc* [1996] 673 A 2d 148 (Delaware); *Queensland Mines Ltd v Hudson* [1978] 18 ALR 1 (PC); *Island Export Finance v Umunna* [1986] BCLC 460; *Balston Ltd v Headline Filters Ltd* [1987] FSR 330.)


**17.3 The ‘no unauthorised profits’ rule**

This rule is a sub-rule of the no conflict rule. A principal may remunerate her fiduciary or expressly allow her to retain any incidental profits acquired in the course of carrying out her fiduciary duties. However, if fiduciaries were allowed to retain unauthorised or ‘secret’ profits, the fiduciary’s interest would be to seek out and obtain those and this would be in conflict with her interest to act only in the best interests of her principal (*Bray v Ford* [1896] 2 AC 46). Most fiduciaries are, of course, authorised to receive some payments in connection with their work. Directors and agents are typically paid for their services. Most trust instruments contain charging clauses entitling the trustees to be paid on an ongoing basis out of the trust funds.†

A fiduciary will be stripped of any unauthorised profits made in breach of fiduciary duty, through either a personal liability to account for them to the principal or a constructive trust of them in favour of the principal. There has been a long-running debate about which of these responses is appropriate, a debate which was played out in *Lister & Co v Stubbs* (1890) 45 Ch D 1 (CA), *A-G Hong Kong v Reid* [1993] UKPC 2, [1994] 1 AC 324, and *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347, [2012] Ch 453, and resolved in *FHR European Ventures LLP v Cedar Capital Partners LLC* [2014] UKSC 45, [2014] 4 All ER 79, [2014] 3 WLR 535. This is discussed in the next chapter.

The sorts of cases in which incidental profits may arise are numerous. Where a trust has a majority shareholding in a company, and the trustees use their voting power to become appointed as directors, they may not keep for themselves any fees earned as directors, unless they are authorised to do so: *Re Macadam* [1946] Ch 73. In *Williams v Barton* [1927] 2 Ch 9, the trustee received a commission from a brokerage firm for introducing new clients to them, and he was liable to the trust for the commission he received for bringing in the trust business. A trustee will be stripped of any profits earned by engaging in business in competition with that of the trust: *Re Thomson’s Settlement* [1986] Ch 99. For obvious reasons, a fiduciary will be stripped of any bribe accepted to exercise their fiduciary powers for the advantage of the bribe-payer: *A-G for Hong Kong v Reid; Islamic Republic of Iran Shipping Lines v Denby* [1987] 1 Lloyd’s Rep 367.

**SELF-ASSESSMENT QUESTION**

1. To which of the following profits does the ‘no unauthorised profits’ rule apply?

   a. Director’s fees earned by a trustee elected to represent the trust’s share-holding.

   b. A company agent’s year-end performance bonus.

   c. A bribe paid to a solicitor to settle a case on favourable terms.

   d. Payments made to the trustee out of the trust fund under the trustee charging clause in the trust instrument.

   e. A secret commission paid by a vendor to a purchaser’s agent.

**17.4 The ‘self-dealing’ rule**

If a fiduciary buys assets from their principal or sells them to the principal within the fiduciary’s powers under the trust or contract of agency, they are clearly acting in conflict of interest, for the fiduciary takes up roles on both sides of the contract, as both buyer and seller. For this reason, the purchase by a trustee of trust assets, or a sale to the trust of the trustee’s own assets, may be set aside on the application of a beneficiary, regardless of the fairness of the sale, unless the trustee was expressly authorised to enter into such a transaction. A purchase by the fiduciary of the principal’s rights is the central case in which the self-dealing rule applies, but the rule is now said to apply not only to purchases but to any transaction which cannot be effected without the concurrence of the fiduciary, including the grant of a lease of trust property or even the consent by a trustee-landlord to an assignment of a lease: see *Re Thompson’s Settlement* [1986] Ch 99. The rule applies not only where a

† See Duke of Norfolk’s Settlement Trusts [1982] Ch 61 for a discussion of the circumstances in which a trustee can apply for increased remuneration beyond that provided for in the trust instrument.
fiduciary enters into a transaction in their own name, but also through a nominee, or partnership, or company of which the trustee is a director.

The remedies available to the beneficiaries depend on whether the contract of sale is still executory (i.e. not yet performed) or performed, and if performed, whether the right has been sold to a \textit{bona fide} purchaser or not. If the contract has not yet been performed, the fiduciary is not allowed to perform it. Where the contract has been performed and the fiduciary has the right still in their hands, or it is in the hands of a third party who is not a \textit{bona fide} purchaser for value, the fiduciary or third party must reverse the transaction and restore the prior situation. If the transaction cannot be reversed, perhaps because the fiduciary has sold the assets on to a \textit{bona fide} purchaser, the fiduciary will be liable for any profits made from the sale. If it can be shown that the right was sold on at an undervalue, the fiduciary will be liable for the profit that should have been earned. In short, where a transaction cannot be reversed, the trustee will be required to pay to the principal an amount calculated to ensure that the principal receives the full market value of the right in question.

\textbf{Activity 17.3}

Read \textit{Holder v Holder} [1968] Ch 353, and explain why the self-dealing rule was not applied in that case.

\textbf{17.5 The ‘fair-dealing’ rule}

The fair-dealing rule applies to transactions in which the fiduciary purchases from the principal assets over which the fiduciary has some control. The classic example is a trustee who purchases the interest under the trust of one of the beneficiaries. A non-trustee example is where a manager of a block of flats offers to buy the freehold title from the landlord. Notice that in these cases, unlike the cases to which the self-dealing rule applies, there really are two parties to the transaction: the fiduciary cannot act as both vendor and purchaser, but must deal with the principal to complete the transaction. Thus the danger is less.

The rationale behind the rule is that having dealt with the assets in question in the past, the fiduciary is probably in a better position to negotiate, knowing more about their value, and so on. Of course, in entering into such a transaction, the fiduciary’s own interests are in conflict with those of the principal. Notice that the rule applies only to transactions concerning assets which are the subject-matter of a trust or business in which the fiduciary acts for the principal.

Under the fair-dealing rule the fiduciary has the burden of proof (\textit{Re Thompson’s Settlement}) to show that:

- the fiduciary did not take advantage of their position
- the fiduciary disclosed all relevant information to the principal
- the beneficiary did not rely solely on the fiduciary’s advice to enter into the transaction, and
- the price was fair.

Where the fair-dealing rule applies to impeach a transaction, the remedies are the same as in the self-dealing case. The transaction can be set aside if possible, and if not (typically because the asset has been sold on to a \textit{bona fide} purchaser for value), then the fiduciary will be liable to pay an amount to ensure that the principal receives its full market value.

\textbf{Activity 17.4}

State whether the self-dealing rule, the fair-dealing rule, or neither, applies to the following transactions:

a. A trustee sells her shares in XYZ plc to the trust.

b. An agent for an antiques dealer offers to buy the latter’s antiques business.
c. A trustee pays an income beneficiary £10,000 to purchase the beneficiary’s right to income under the trust for the next 10 years.

d. A solicitor buys a painting from Jonah, for whom he acted in divorce proceedings.

e. A director of ABC Ltd enters into a contract on its behalf for the purchase of raw materials from XYZ Ltd, a private company she owns.

17.6 Equitable compensation for breach of fiduciary obligation

As we have seen, the first approach to equity in the case of a breach of fiduciary obligation is to attempt to reverse the breaching transaction, to set aside a self-dealing or fair-dealing sale, or to make the fiduciary treat an unauthorised profit as if they held it on trust for the principal. But in certain circumstances that will be impossible. If, for example, in breach of fiduciary duty, a solicitor advised a client to enter into a transaction which turned out to be financially disastrous, the transaction is not reversible by the solicitor, because the solicitor did not enter into it. All the client can do is seek compensation for the loss suffered because of following the solicitor’s tainted advice. In such a case, the client will make a claim for equitable compensation (i.e. the equivalent to damages at common law for a tort or breach of contract, as discussed in the previous chapter).

The leading case is Nocton v Ashburton [1914] AC 932. The plaintiff claimed that his solicitor, in breach of fiduciary duty, advised him to release a security interest, which advice he followed. The transaction was in furtherance of a land development scheme, and the solicitor’s advice was given in conflict of interest: the release of the security would increase the possibility of the solicitor realising his own investment in the scheme, whereas in doing so the risk that the plaintiff’s personal liability if the scheme went awry (which it did) was increased. The House of Lords held that the solicitor must compensate the plaintiff for his loss.

As we have seen (Section 16.2.1), the principles regarding causation of loss have been held in the House of Lords to be different from common law principles. The equitable principles are designed ‘to make good a loss in fact suffered by the beneficiaries, which using hindsight and common sense, can be seen to have been caused by the breach’ (Target Holdings Ltd v Redfern [1995] UKHL 10, [1996] AC 421, per Lord Browne-Wilkinson). Two cases where these principles were applied to a breach of fiduciary obligation are Canson Enterprises Ltd v Boughton & Co [1991] 3 SCR 534, 85 DLR (4th) 129, a Canadian case discussed in Target Holdings, and Swindle v Harrison [1997] 4 All ER 705 (CA). In Canson, a solicitor breached his fiduciary duty to his client, whom he advised in a land title purchase, by failing to inform it that the vendors had made an improper profit. It was established that, had the client known about this, it would have withdrawn from the purchase. The client went on to build a warehouse on the land, and because of the negligence of its builders and engineers, the warehouse was defective, leading to a large financial loss. The client sued the solicitor for the loss, arguing that had the solicitor complied with his duty, the client would not have purchased the land, and then gone on to develop it with such disastrous results. The question was whether the solicitor’s breach of duty caused the client’s loss.

In Swindle v Harrison, a solicitor (the unfortunately named Mr Swindle) arranged bridging finance to purchase land of a client, but breached his fiduciary duty to her by failing to tell her that he received a commission for so doing. The bridging finance permitted her to purchase the title, on which land she briefly ran a hotel and restaurant business that failed, causing her loss. She sued the solicitor, claiming that his breach of duty had caused the loss on the basis that had he not arranged the bridging finance (in the course of doing which he breached his fiduciary duty to her), she would not have been able to purchase the property, start the business, and suffer the loss. Not surprisingly, the claims in both cases failed, and for what appear to be obvious reasons. Although the losses for which compensation was sought might not have happened ‘but for’ the defendant’s breach, they did not flow from the breach
in the sense of being caused by it. In *Canson*, the obvious cause of the loss was the negligence of the plaintiff's builders and engineers, and in *Swindle*, it was caused by the plaintiff's decision to run the business and failure to run it properly.

It would appear that the reason why these plaintiffs thought it possible to claim for these losses was that the principles of causation that apply to the award of equitable compensation have been thought to be more flexible and generous to claimants than common law principles.

**Summary**

The fair-dealing rule applies to transactions in which the fiduciary has some control over the principal's assets in their fiduciary role and purchases them from the principal. Since there are two parties to the transactions, the danger here is less than in the self-dealing rule. The rule only arises concerning assets which are the subject of a trust or a business in which the fiduciary acts for the principal. The transaction will be a breach of the fair-dealing rule if the fiduciary cannot show that:

- they have not taken advantage of their position
- they have disclosed all the relevant information to their principal
- the principal did not solely rely on the fiduciary's advice to enter into the transaction
- the price was fair.

In certain circumstances the breaching transaction cannot be reversed and so a different remedy is required. The principal will have to make a claim for equitable compensation. Although the rules for causation of loss are thought to be more generous than the common law rules, *Canson Enterprises Ltd v Boughton & Co* and *Swindle v Harrison* appear to show otherwise. In both cases, the principal's claims failed even though the losses for which compensation was claimed would not have happened ‘but for’ the defendant's breach, but they still did not flow from the breach in the sense of being caused by it.

### 17.7 The uncertain application of trustee exemption clauses

Recall *Armitage v Nurse* [1997] EWCA Civ 1279, [1998] Ch 241 (Section 16.3.3), which explains the valid scope of trustee exemption clauses. Unfortunately, the case is unclear as to the application of such clauses to breaches of fiduciary obligations. You will recall that Millett LJ regarded the core obligations of trustees as including a duty of loyalty, which suggests that fiduciary obligations are core obligations that cannot be covered by an exemption clause. However, the judgment does not actually say that. In particular, it focuses on the trustee's actual state of mind, holding that a clause cannot exempt liability for intentionally fraudulent or reckless acts. As we have seen (Section 17.2), breaches of fiduciary obligation do not necessarily involve dishonesty or recklessness. The defendant in *Boardman* was liable even though his intentions were wholly honest. Millett LJ specifically declined to discuss the application of such clauses to different sorts of breach of fiduciary obligation in detail, as no such conduct was pleaded by the plaintiff. As a consequence, the limits of trustee exemption clauses remain uncertain.

**Self-assessment questions**

1. In a trust, who is the fiduciary?
2. State the ‘no conflict’ rule as simply as you can.
3. What is the ‘no unauthorised profits’ rule?
4. What was the breach of fiduciary duty in *Swindle v Harrison*?
5. A trustee buys a title to a second-hand car from the trust. What rules does this breach, if any?
6. A trustee buys a second-hand car from one of the beneficiaries of the trust. What rules does this breach, if any?

**ESSENTIAL READING**

At least one of the following:

- Martin, Chapter 21: ‘The fiduciary nature of trusteeship’.
- Oakley, Chapter 10: ‘Constructive trusts’, Section II ‘Advantages obtained by fiduciaries breaching their duty of loyalty’.
- Pettit, Chapter 8: ‘Constructive trusts’, Section 2 ‘Obligation to account as a constructive trustee for profits received by virtue of his position as trustee’.

**FURTHER READING**


**SAMPLE EXAMINATION QUESTIONS**

**Question 1** Richard managed Paul’s pub. In January, he fired the regular Friday night disc jockey in order to hire his brother, who goes by the professional name of ‘Slammer’. Even though Slammer is inexperienced, Richard paid him twice what he paid the old disc jockey. In February, he changed the beer supplier, accepting a £2,000 ‘signing bonus’ from the new supplier, which he invested in shares now worth £3,000. In March, Richard persuaded Paul to sell the pub to him. Richard’s accounts for the pub business were in disarray, so it was difficult to value the business, but Paul accepted Richard’s estimate as to the pub’s profitability and on that basis sold the pub to him for £150,000. In April, Richard sold the pub to a large brewer for £300,000. Advise Paul.

**Question 2** ‘A fiduciary obligation is difficult to define, but a breach of fiduciary obligation is easy to spot, which is why the content of fiduciary obligations is best understood by looking at the various cases in which they are breached.’ Discuss.

**Question 3** Fred was recruited by Massive Music Ltd (MML) to scout for new talent. He was told by his friend, Susan, an employee of Rage Records plc (RRP), that a new band in Scotland, Pot of Gold, was worth investigating. Paying for his flight on his MML expense account, Fred listened to and interviewed the band with a view to signing them with MML. The band members adamantly refused to sign with MML because of its English origins, but indicated they would sign with RRP, a global US-based company. Fred arranged to sign them with RRP instead, collecting a £50,000 fee from RRP, which he used to pay off his mortgage. Pot of Gold has since made £2.5 million in profits for RRP. Fred did, however, sign his brother, Liam, to a lucrative contract with MML, which was unaware that Liam was Fred’s brother. MML lost £500,000 recording and promoting Liam, whose contract was terminated. Advise MML.

**ADVICE ON ANSWERING THE QUESTIONS**

**Question 1** This is a straightforward question involving several breaches of fiduciary obligations. In making the decision to fire the former DJ and hire his brother at twice the salary, Richard favours the interests of a third party (his brother) over the interests of Paul. The transaction cannot be ‘reversed’ in the typical sense, since the transaction did not involve a transfer of rights. Paul can claim that Richard compensates him for any losses caused by the decision, in particular the cost of Slammer’s salary in excess of what an inexperienced DJ’s services are worth. If Slammer’s hiring can be shown to have led to a decline in business, that loss can also be claimed. Slammer will only be personally liable as a third-party accessory to a breach of Richard’s fiduciary obligation
or as a recipient of payments made in breach of fiduciary obligation if it can be established that he accepted the job dishonestly in the knowledge that Richard ought not to have hired him. The ‘signing bonus’ is clearly an unauthorised profit. If the money is held under a constructive trust (see Section 17.3) its value can be traced into the shares. The purchase of the pub clearly breaches the fair-dealing rule, and Richard will be liable to compensate Paul in the amount of £150,000 so that Paul receives the full market value of the pub. The transaction is unlikely to be reversible as it is very unlikely that the large brewer is not a bona fide purchaser.

**Question 2** A good answer to this question will explore the different rules indicating the way in which fiduciary obligations can be breached (i.e. the no-conflict rule, the no unauthorised profits rule, the self-dealing rule and the fair-dealing rule), and these should be discussed with the aim of explaining how they shape a fiduciary’s duties to their principal. A very good answer will tackle the quotation more directly by proposing a more general explanation or theory of fiduciary obligations which tries to show the common basis for the various rules.

**Question 3** The question concerns the no-conflict rule in the context of a business opportunity. It is clear that the opportunity to recruit Pot of Gold came Fred’s way when he was acting in the capacity of fiduciary to MML. As the decisions in *Keech v Sandford* (1726) and *Industrial Development Consultants Ltd v Cooley* (1972) make clear, the fact that Pot of Gold will not sign with MML under any circumstances does not allow Fred to pursue the opportunity in another way to his own advantage. In such a circumstance, Fred could only proceed by fully informing MML of the situation and gaining their consent to act on his own behalf. As he did not do so, he may be stripped of any profits he acquires from realising the opportunity. Thus he will be required to account for the £50,000 signing fee from RRP, which can be traced into the mortgage payment if held by him on constructive trust (Section 17.3). It is unlikely that RRP will be liable to MML, as it is difficult to see how they could be shown to have acted dishonestly. In *Satnam Investments v Dunlop Heywood* [1999] 3 All ER 652 a third party benefited in its purchase of rights by the plaintiff’s fiduciary’s unauthorised release of confidential information, and the court did not hold it liable, reasoning in part that it would be contrary to commercial good sense to hold competitors liable to each other for the advantages gained from the breach by another’s fiduciary. The signing of Liam was in breach of the no-conflict rule, as with Slammer in Question 1, and Fred will be liable for all of the losses to his principal flowing from this breach, which in this case appears to be £500,000.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

I can explain what fiduciary obligations are, and distinguish them from other obligations a trustee might have.

I can describe the consequences which attach to the receipt by a fiduciary of an unauthorised profit.

I can explain what happens when a trustee purchases trust rights or sells rights to the trust.

I can describe the circumstances in which a trustee may safely purchase the interest of a beneficiary.

I can explain and apply the law governing equitable compensation for breach of fiduciary obligation.

I can explain the uncertainty regarding the application of trustee exemption clauses to a breach of a trustee’s fiduciary obligation.

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

17.1 Fiduciary obligations and ‘conflict of interests’
17.2 The ‘no conflict’ rule
17.3 The ‘no unauthorised profits’ rule
17.4 The ‘self-dealing’ rule
17.5 The ‘fair dealing’ rule
17.6 Equitable compensation for breach of fiduciary obligation
17.7 The uncertain application of trustee exemption clauses
## Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction</td>
<td>200</td>
</tr>
<tr>
<td>18.1 Genuine constructive trusts</td>
<td>201</td>
</tr>
<tr>
<td>18.2 False constructive trusts</td>
<td>201</td>
</tr>
<tr>
<td>18.3 Types of constructive trust</td>
<td>202</td>
</tr>
<tr>
<td>18.4 Making sense of constructive trusts</td>
<td>203</td>
</tr>
<tr>
<td>18.5 Constructive trusts which respond to wrongdoing</td>
<td>203</td>
</tr>
<tr>
<td>Reflect and review</td>
<td>207</td>
</tr>
</tbody>
</table>
Introduction

Much of the material found in textbook chapters entitled 'Constructive Trusts' has already been dealt with in other chapters of this guide. This has to do with the uncertain meaning of 'constructive trust'. What we mean by it in this guide is a trust which arises by operation of law, that is, a trust which the legal system imposes on someone normally without their consent. This is in contrast to an express trust, which arises because a settlor has manifested an intention that a trust come into existence.

As we shall see, many cases which are often labelled 'constructive trusts' are not really constructive trusts at all. Because part of this chapter involves weeding out such trusts, you should review the five chapters of the subject guide listed in the Essential reading now.

**Essential Reading**

Quickly re-read:

- Chapter 3: 'Types of trust'.
- Chapter 6: ‘Creating express trusts II: constitution’.
- Chapter 7: ‘Proving declarations of trust’.
- Chapter 8: ‘Secret trusts’.
- Chapter 16: ‘Breach of trust’.
- Penner, Chapter 4: ‘Constructive trusts’.

**Learning Outcomes**

By the end of this chapter and the relevant readings you should be able to:

- explain why certain trusts which are thought to be constructive are, in reality, express
- explain why ‘constructive trusteeship’ when used to describe the personal liability of third parties is a misleading expression which should be avoided
- explain the controversy over whether the receipt of unauthorised profits by a fiduciary should be held on constructive trust.
18.1 Genuine constructive trusts

The first aim of this chapter is to distinguish genuine cases of constructive trusts from false ones. We begin by describing a few genuine cases, so as to give you a flavour of the subject. In the succeeding section we address cases which are mistakenly thought to be examples of constructive trusts. It is important to note that we are not thereby endorsing the reasoning in either case, but merely using them as illustrations of genuine constructive trusts.

Where the holder of a title to land enters into a contract to sell it to a purchaser, equity will usually enforce that contract specifically. It will also apply the maxim 'equity looks upon that as done which ought to be done' and treat the vendor as holding their title on trust for the purchaser at the moment the contract is formed: *Lysaght v Edwards* (1876) 2 Ch D 499; *Jerome v Kelly* [2004] UKHL 25, [2004] 2 All ER 835, [2004] 1 WLR 1409. There is no declaration of trust on the vendor’s part, so this is a genuine example of a constructive trust.

Recall from Section 6.2.2 that there are a number of circumstances in which equity will perfect imperfect gifts. It generally does so through the imposition of a trust on the donor. So, for example, in *Re Rose* [1952] EWCA Civ 4, a trust was imposed on Mr Rose at the moment he had done what he needed to do to make a gift of shares to his wife even though legal title had not yet passed by registration. There was no declaration of trust on his part, so this too was a genuine example of a constructive trust.

In *FHR European Ventures LLP v Cedar Capital Partners LLC* [2014] UKSC 45, [2014] 4 All ER 79, [2014] 3 WLR 535, a secret commission received by a fiduciary was held on constructive trust for his principal from the moment of receipt. As discussed in the next chapter, there is a controversy over whether a constructive trust should have been imposed in this situation, but there is no doubt that the trust imposed was a true constructive trust. A similar controversy surrounds the trust of a mistaken payment imposed in *Chase Manhattan Bank NA v Israel-British Bank (London) Ltd* [1981] Ch 105 (also discussed in the next chapter), but there is no doubt that it was a true trust arising by operation of law.

18.2 False constructive trusts

As we saw in Section 16.4, there are a number of circumstances in which third parties involved in a breach of trust are held to be ‘liable to account as constructive trustees’, that is, they are personally liable to restore the trust with money from their own pockets ‘as if they were a trustee’. As this is only a personal liability, there are no rights being held on trust. The label ‘constructive trustee’ is potentially confusing because it can mean either someone who is (a) not a trustee, but being treated as one, or (b) an actual trustee of a constructive trust. For this reason, this usage is frowned upon, and in *Dubai Aluminium Co Ltd v Salaam* [2002] UKHL 48, [2003] 2 AC 366, Lord Millett suggested that the language of constructive trusteeship should be jettisoned and the defendant described simply as ‘liable to account in equity’. One might ask, in the light of the fact that the duty to give an ‘account’ is also fictitious in such circumstances, whether the courts should not go further and simply describe the liability as one to pay damages, for that is what it seems to be.

In *Williams v Central Bank of Nigeria* [2014] UKSC 10, a majority of the Supreme Court decided that dishonest assistants and knowing recipients are not constructive trustees for the purposes of the Limitation Act 1980. We are not concerned with the limitation issue, but with what the judgments tell us about the nature of the liability for assisting a breach of trust or receiving assets in breach of trust. At [9], Lord Sumption distinguished between those constructive trustees who ‘are true trustees’ and those who are not:

In its second meaning, the phrase ‘constructive trustee’ refers to something else. It comprises persons who never assumed and never intended to assume the status of a trustee, whether formally or informally, but have exposed themselves to equitable
It is notable that he did not distinguish between assistants and recipients in this context, since the latter will have to be holding trust assets when liability arises.

As we saw in Chapter 3, an express trust is synonymous with a declared trust, for what is expressed in an express trust is a declaration of trust. We also saw that, in certain cases, the legislature has restricted the type of evidence which courts are allowed to admit to prove that such a declaration has occurred, specifically in cases of alleged declarations of trust of land (LPA 1925, s.53(1)(b)) and testamentary trusts (Wills Act 1837, s.9). As we also saw in Chapter 7, courts will sometimes admit such evidence regardless, thereby allowing the allegation of a declaration of trust to be made good. In *Rochefoucauld v Boustead* [1897] 1 Ch 196 (CA), the trust imposed was clearly identified by the court as an express trust, but has often been treated as constructive by subsequent courts and commentators. As discussed in Chapter 8, there is a debate over whether secret trusts should be classified as express or constructive.

**Self-assessment questions**

1. Why are trusts enforced despite the lack of admissible evidence under s.53(1)(b) of the Law of Property Act 1925 or s.9 of the Wills Act 1837?
2. Why is the term ‘liable to account as a constructive trustee’, when used to describe the personal liability of third parties in cases of breach of trust, potentially misleading?

### 18.3 Types of constructive trust

Having now expelled the false ‘constructive trusts’, it is time to move to the genuine article. And in this respect, the most important question one can ask about constructive trusts is why they arise. To say that they are imposed by courts without the right-holder’s consent tells us only that they do not arise because of a declaration of trust. The question why they arise will be addressed in the rest of this chapter and the next. Before doing so, we need to consider two different types of constructive trust: the ‘institutional’ constructive trust and the ‘remedial’ constructive trust. Much confusion will be avoided if we make clear at the outset what these terms mean. Unfortunately, the only way to understand the terminology is to realise that the words do not mean what they say.

#### 18.3.1 Institutional constructive trusts

The vendor-purchaser constructive trust and the *Re Rose* constructive trust are both regarded as institutional constructive trusts. This means that they arise because of the application of rules, not by order of the court. The trust arises by operation of law in response to relevant facts, and the court declares that this has happened. Even though we might criticise the imposition of a trust in such cases, we can at least predict with some certainty when such a trust will arise, and moreover, engage in meaningful debate over the reasoning of the judges who lay down the rules which trigger such trusts.

#### 18.3.2 Remedial constructive trusts

The first thing to note is that the phrase ‘remedial constructive trust’ does not refer to the personal liability to account as a constructive trustee. As we have seen, although this liability might be thought of as remedial, it does not give rise to a trust. A remedial constructive trust, by contrast, really is a trust. In what way, therefore, does it differ from its institutional counterpart? The explanation is that it does not arise through
the application of rules but through the exercise of judicial discretion, one concerned with notions of fairness in the individual circumstances. As such, it offends the constitutional principle of the rule of law, and it is not surprising to find our courts rejecting it on a number of occasions, most notably by the House of Lords in Pettitt v Pettitt [1969] UKHL 5, [1970] AC 777 and Gissing v Gissing [1970] UKHL 3, [1971] AC 886, by the Privy Council in Re Goldcorp Exchange Ltd [1994] UKPC 3, [1995] 1 AC 74, and by the Court of Appeal in Polly Peck International plc v Nadir (No 2) [1992] EWCA Civ 3, [1992] 4 All ER 769 and Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd [2011] EWCA Civ 347, [2012] Ch 453. Indeed, in Polly Peck, Mummery LJ said that the idea that English law could have a remedial constructive trust was ‘inconceivable’.

However, there are some signs of such a trust, at least at the level of the Court of Appeal, where recent cases seem to be being decided on the ground of nothing more than ‘unconscionability’. The worst offender in this regard is Pennington v Waine [2002] EWCA Civ 227, [2002] 4 All ER 215, [2002] 1 WLR 2075, though it is far from alone. We can only hope that this trend will not survive the scrutiny of the Supreme Court, though the decisions of the House in Stack v Dowden [2007] UKHL 17, [2007] 2 AC 432 and the Supreme Court in Jones v Kernott [2011] UKSC 53, [2011] 3 WLR 1121 do not give much cause for optimism in this regard.

18.4 Making sense of constructive trusts

On the basis that English law knows only the institutional constructive trust, a trust arising through the application of rules and one not because of a declaration of trust, the question is whether it is possible to make sense of such trusts. As we have seen, to say that a trust is constructive (i.e. that it arises by operation of law), gives us only negative information, that it arises for a reason other than an effective declaration of trust. Is it possible to identify the reasons why such trusts arise?

Professor Birks famously suggested that rights (including trusts) arise in response to events which happen in the world. So, for example, if I punch you on the nose (event), the law gives you a right to damages against me (response).

The events giving rise to rights can be subdivided into four main categories: (1) manifestations of consent, (2) wrongs, (3) unjust enrichments, and (4) other miscellaneous events. The punch on the nose, for example, was a wrong. The most common event generating rights is a manifestation of consent, and there is no doubt that most trusts arise because of such manifestations of consent; we call these express trusts. Events 2, 3 and 4 might then be described as events which give rise to rights by operation of law. The question we will ask is which constructive trusts belong in which category. This will help us develop a critical approach to this topic. We start with wrongdoing, which will occupy the rest of this chapter. The other headings, unjust enrichment and miscellaneous other events, will be discussed in the next chapter. Indeed, you will not obtain a clear understanding of this subject until you have studied that chapter as well, and you may find it easier to wait until you have finished both chapters before attempting to answer any questions.

18.5 Constructive trusts which respond to wrongdoing

The usual response to wrongdoing, both at law and equity, is the award to its victim of a monetary remedy. At common law, we call this damages. In equity, it goes, as we have seen, by the confusing name of a ‘liability to account as a constructive trustee’ or sometimes ‘equitable compensation’. For most legal or equitable wrongs, there is no possibility of a trust. So, for example, where a defendant is liable for dishonestly assisting a trustee to commit a breach of trust, the defendant will have no particular asset in their hands which the beneficiary can claim is held for them on trust. But in some cases, an asset will have been received as a consequence of the wrong, and the question is whether the court will say that it is held by the wrongdoer on trust for their victim (or their victim’s estate).
A constructive trust can arise when one joint tenant murders the other and thereby acquires sole legal ownership by way of survivorship. The murderer will hold title on constructive trust for themself and their victim's estate in equal shares. This rule also applies in cases of manslaughter. It also applies when there are more than two joint tenants, although it does not affect the rights to survivorship of the innocent joint tenants: see *Troja v Troja* (1994) 33 NSWLR 269 (CA). Under the Forfeiture Act 1982, the court has the power to modify the rule: see *Dunbar v Plant* [1997] EWCA Civ 2167, [1998] Ch 412.

A constructive trust can also arise in response to the equitable wrong of breach of fiduciary duty but is more controversial. If in breach of fiduciary duty a fiduciary takes a bribe, do they merely owe the amount of the bribe to their principal (i.e. is accountable as a constructive trustee) or do they hold it, or its traceable proceeds, on trust for him? In *Lister v Stubbs* (1890) 45 Ch D 1, the Court of Appeal held that any argument for a trust in such circumstances confused two different things, ownership with obligation. Although a debt of £1 was created for every £1 the dishonest fiduciary received as a bribe, the relationship never become one of trustee and beneficiary. In other words, although there was a liability to account as a constructive trustee, the defendant was not in fact a trustee at all.

Despite this very clear view, later courts have muddled the waters by appearing to hold that there will indeed be a constructive trust in such circumstances (*Williams v Barton* [1927] 2 Ch 9; *Boardman v Phipps* [1966] UKHL 2, [1967] 2 AC 46, per Lord Guest; *Industrial Development Consultants Ltd v Cooley* [1972] 1 WLR 443). In none of them, however, was the point argued, so they do not provide clear authority in this regard. In all of them, a personal claim would have sufficed.

However, in the Privy Council decision in *A-G for Hong Kong v Reid* [1993] UKPC 2, [1994] 1 AC 324, a case briefly mentioned in Chapter 3, the point was fully argued, and the opposite view taken in a decision given by Lord Templeman. Beginning with the uncontroversial proposition that the fiduciary was a debtor in equity for the amount of the bribe, he said:

> Equity considers as done that which ought to have been done. As soon as the bribe was received, whether in cash or in kind, the false fiduciary held the bribe on constructive trust for the person injured.

As we will see in the next chapter, this is probably a misuse of the maxim involved in the vendor-purchaser constructive trust, for two reasons. First, what should have been done was that Reid, the false fiduciary, not take the bribes in the first place. However, if we deem Mr Reid never to have taken bribes, there would not even be a personal claim to his gains. By contrast, the vendor-purchaser constructive trust arises because of the fictionalised performance of the primary obligation of the vendor to perform their promise, not their secondary obligation to pay damages for a failure to perform that promise. It is not therefore a doctrine which applies to wrongdoing at all. A second and more substantial objection is that the argument mistakes the nature of the duty to account. As we saw in the last chapter, this is fictional language for an obligation to pay money. But the money can be taken from any source belonging to the person liable to account. It is not, unlike an agreement to sell title to a particular plot of land, an obligation to transfer any right in specie, and it is for that further reason that the vendor-purchaser constructive trust can also have no application in a case such as *Reid*.

Lord Millett is a strong supporter of *Reid*. Writing extra-judicially, he argued that 'the fiduciary is bound to pay the bribe to his principal the moment he receives it' and a constructive trust ‘arises whenever a person receives money or property in circumstances which make it unconscionable for him to treat it as his own’: ‘Bribes and secret commissions again’ (2012) 71 CLJ 583, 592–93. He also said (at 591):

> Although the bribe was paid to the fiduciary for his own use and benefit, he is treated as receiving it with the authority of his principal and for the principal’s account. The fiduciary is not allowed to say that he received the bribe for his own benefit.
In *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* [2011] EWCA Civ 347, [2012] Ch 453, the Court of Appeal decided that it was bound by its own previous decisions in *Metropolitan Bank v Heiron* (1880) 5 Ex D 319, *Lister & Co v Stubbs* (1890) 45 Ch D 1, and three other cases to hold that the receipt of a bribe does not normally give rise to a constructive trust. This is contrary to the Privy Council’s advice in *A-G Hong Kong v Reid*, on appeal from New Zealand, which had been widely regarded as also representing the law in England and Wales. Reid had also been followed in Singapore and British Columbia: *Sumitomo Bank Ltd v Kartika Ratna Thahir* [1992] SGHC 301, [1993] 1 SLR 735; *Insurance Corp of British Columbia v Lo*, 2006 BCCA 584, 278 DLR (4th) 148. In *Sinclair*, the Court of Appeal proceeded on the basis that bribes were no different from other secret profits obtained by in breach of fiduciary duty, and said (at [88]):

[A] beneficiary of a fiduciary’s duties cannot claim a proprietary interest, but is entitled to an equitable account, in respect of any money or asset acquired by a fiduciary in breach of his duties to the beneficiary, unless the asset or money is or has been beneficially the property of the beneficiary or the trustee acquired the asset or money by taking advantage of an opportunity or right which was properly that of the beneficiary, unless the asset or money is or has been beneficially the property of the beneficiary or the trustee acquired the asset or money by taking advantage of an opportunity or right which was properly that of the beneficiary.

The Federal Court of Australia chose not to follow *Sinclair*, but held that a remedial constructive trust was available if needed ‘to achieve “practical justice” in the circumstances’: *Grimaldi v Chameleon Mining NL (No 2)* [2012] FCAFC 6 at [583].

In *FHR European Ventures LLP v Mankarious* [2013] EWCA Civ 17, [2014] Ch 1, the Court of Appeal followed *Sinclair*, as it was bound to do, but with some unease. It concluded that the agent in that case held a secret commission in trust for its principal because it had taken advantage of an opportunity that belonged to the principal. The Supreme Court affirmed the judgment, but on the basis that all bribes and secret commissions received by an agent are held on constructive trust for the principal: *FHR European Ventures LLP v Cedar Capital Partners LLC* [2014] UKSC 45, [2014] 4 All ER 79, [2014] 3 WLR 535. In other words, *Lister & Co v Stubbs* and *Sinclair* were overruled. Lord Neuberger said at [46] that ‘considerations of practicality and principle … appear to support the respondents’ case, namely that a bribe or secret commission accepted by an agent is held on trust for his principal’.

**Activity 18.1**

Read *Lister & Co v Stubbs*, *A-G for Hong Kong v Reid*, *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd*, and *FHR European Ventures LLP v Mankarious*. Explain the difference between the decisions and the courts’ reasoning.

**Essential reading**

At least one of the following:

- Martin, Chapter 12: ‘Constructive trusts’.
- Oakley, Chapter 10: ‘Constructive trusts’.
- Pettit, Chapter 8: ‘Constructive trusts’.

**Further reading**


Hayton & Mitchell, Chapter 15: ‘Constructive trusts’.


Penner, J.E. ‘The difficult doctrinal basis for the fiduciary’s proprietary liability to account for bribes’ (2012) 18 Trusts & Trustees 1000.


SAMPLE EXAMINATION QUESTION

What is a constructive trust?

ADVICE ON ANSWERING THE QUESTION

At first glance, this might seem like a simple question, requiring nothing more than a definition such as ‘a constructive trust is a trust which arises by operation of law’. While correct, it is clearly insufficient, for properly understood the question requires you to consider when and why constructive trusts arise by operation of law. This requires a survey of those circumstances in which they arise (and for this you will also need to make reference to the next chapter), and those circumstances where they are mistakenly thought to arise.

The best way to approach such a question is to remember the cases and texts you have read, and try to produce some ideas about why constructive trusts arise in the wide disparity of circumstances in which they do. It is perfectly sensible to claim that constructive trusts arise in response to different fact situations to advance different policies of the law, or to respond to different aspects of justice. Compare, for example, the rationale that might lie behind the constructive trust that converts a contractual obligation to convey land into a constructive trust for the purchaser, with the constructive trust that allows a beneficiary of trusts to make a proprietary claim against the traceable proceeds of trust property held by a third-party recipient in the case of a breach of trust (see Chapter 19).

Finally, it is important to include some discussion of the constructive trust that may or may not properly arise over an unauthorised profit of a fiduciary. In recent years this has generated the most controversy, and you should try to take a view on this issue, giving your reasons of course. You will not be penalised for adopting a view that differs from the Examiners’, but you do need to take seriously the arguments for and against.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th></th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td>I can explain why certain trusts which are thought to be constructive are, in reality, express.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain why ‘constructive trusteeship’ when used to describe the personal liability of third parties is a misleading expression which should be avoided.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can explain the controversy over whether the receipt of unauthorised profits by a fiduciary should be held on constructive trust.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Section</th>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td>18.1 Some genuine examples of constructive trusts</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18.2 False constructive trusts</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18.3 Types of constructive trust</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18.4 Making sense of constructive trusts</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18.5 Constructive trusts which respond to wrongdoing</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Introduction ................................................................. 210

19.1 Constructive trusts as a response to unjust enrichment .... 211

19.2 Constructive trusts responding to other miscellaneous events. 212

Reflect and review ...................................................... 221

Contents
Introduction

This chapter is a continuation of the last. We have been asking why constructive trusts arise, and have seen that some, such as that in *FHR European Ventures LLP v Cedar Capital Partners LLC* [2014] UKSC 45, [2014] 4 All ER 79, [2014] 3 WLR 535, respond to the event of wrongdoing.

We continue our enquiry by asking whether any constructive trusts can be explained as a response to unjust enrichment, and then whether there are other events that give rise to constructive trusts beyond the two nominate heads of wrongs and unjust enrichment. Within the miscellany, detailed attention is paid to the mysteries of ‘tracing’.

**Essential reading**


**Learning outcomes**

By the end of this chapter and the relevant readings you should be able to:

- explain how some trusts can be seen as responses to a defendant’s unjust enrichment
- define the circumstances in which constructive trusts will arise in circumstances which involve neither wrongdoing nor unjust enrichment
- define the difference between following, tracing and claiming
- explain why the law of tracing often falls into the law of trusts
- explain when the common law does not allow a title holder to trace
- understand and apply the rules governing tracing through mixtures
- explain what backwards tracing is and why the law regarding it is unsettled
- outline the proprietary and personal claims that can arise following the tracing process
- show how rights to subrogation can arise following the tracing process.
19.1 Constructive trusts as a response to unjust enrichment

Like wrongdoing, the most common response to unjust enrichment is the award to the claimant of a money payment from the defendant. Thus, if I pay you £100 by mistake, the common law says that, provided certain conditions are met, you owe me £100. The same view is taken by equity. Thus, if by the exercise of undue influence, I make a gift to you of £100, you will be ‘liable to account’ for that money to me. You will, in other words, be a debtor in equity to me in the sum of £100. The question is whether in either case I can claim that you hold the £100 or its traceable proceeds for me under a constructive trust.

19.1.1 Mistaken payments

In Chase Manhattan Bank v Israel-British Bank London Ltd [1981] Ch 105, a case we first encountered in Chapter 3, Goulding J answered the question in the affirmative, at least in the case of a mistaken payment. But why did such a trust arise? According to Goulding J, it was because the mistaken payer retained the equitable property in the money paid, and since equitable property was held by the payer while legal property was held by the recipient, the consequence was a trust which arose by operation of law.

The problem with this reasoning is that it is premised on the existence of equitable property separate from legal property prior to the mistaken transfer. As we saw in the discussion of the resulting trust (in Chapter 12), this is not correct. There is no pre-existing equitable interest. If a trust arises, an equitable interest arises for the first time. For this reason, the analysis of Goulding J was rightly disapproved by Lord Browne-Wilkinson in Westdeutsche Landesbank Girozentrale v Islington LBC [1996] UKHL 12, [1996] AC 669.

19.1.2 Resulting trusts

As we also saw in Chapter 12, the resulting trusts arise by operation of law and can be regarded as a sub-species of the constructive trust. The question is why they arise. We saw that the explanation proffered by Lords Upjohn and Wilberforce was that it was triggered by the retention by the transferor of his equitable interest in the rights transferred to the transferee. This explanation, however, does not work for precisely the same reason as Goulding J’s reasoning in Chase Manhattan. Birks and Chambers have argued that all resulting trusts arise to reverse the unjust enrichment of the recipient. Although it may well be correct to say that the recipient is thereby unjustly enriched, what still needs to be explained is why the law gives the transferor the benefit of a trust in addition to a personal claim to recover the value of the right transferred. Why is one creditor being treated more favourably than the rest?

19.1.3 Other instances of unjust enrichment

There is no doubt that there are other instances of constructive trusts which can be explained as responses to unjust enrichment. Thus, in Allcard v Skinner (1887) 36 ChD 145, Cotton LJ said that rights transferred because of the undue influence of the transferee were held on trust for the transferor. You should, however, note that this was a minority opinion. The majority said that the plaintiff had only a right to rescind the transfer and thereby create a trust in her favour, a weaker species of right. It is also important to note that Cotton LJ’s reasoning seems to depend on some theory of equitable retention.
19.2 Constructive trusts responding to other miscellaneous events

Those constructive trusts which do not respond to either wrongdoing or unjust enrichment must by definition fall within this last category, and there is no doubt that it has content. Indeed, the vast majority of constructive trusts are to be found here. There is no space to cover them all. Instead, a list of the main incidences is provided, along with a detailed discussion of an area of law called ‘tracing’, by which rights in substitute assets are created when the original assets are substituted in an unauthorised fashion for other rights.

19.2.1 Examples other than unauthorised substitutions

The vast majority of constructive trusts belong in this category. Here is an incomplete list of the situations in which they arise:

- specifically enforceable contracts to transfer interests in land ([Lysaght v Edwards (1876) 2 Ch D 499; Jerome v Kelly [2004] UKHL 25, [2004] 2 All ER 835])
- incomplete gifts of land or company shares ([Re Rose [1952] EWCA Civ 4, [1952] Ch 499; Mascall v Mascall [1984] EWCA Civ 10, 50 P & CR 119])
- mutual wills ([Walters v Olins [2008] EWCA Civ 782, [2009] Ch 212])
- proprietary estoppel ([Thorner v Major [2009] UKHL 18, [2009] 1 WLR 776])

If secret trusts are constructive, they belong here as well. Some of these trusts are discussed in this subject (in Chapters 6, 7, and 8) and others are encountered in Property law. None of them can be explained as responses to wrongdoing or unjust enrichment. Elias calls them ‘perfectionary’, by which he means that they arise to perfect unperfected promises or intentions to benefit others: *Explaining constructive trusts* (Oxford: Clarendon Press, 1990). This distinguishes them from ‘restitutionary’ trusts which arise to compel people to give up assets acquired either wrongfully or as an unjust enrichment.

A difficult issue is why trusts are imposed in the situations listed above. Detrimental reliance is an important factor in the proprietary estoppel cases and possibly also relevant for some of the others. You will need to consider why incomplete gifts are sometimes held on constructive trust. You will also need to consider the reasons why secret trusts arise (if they are constructive) or why they are enforced despite the Wills Act 1837 (if they are express).

19.2.2 Unauthorised substitutions (tracing)

We now come to tracing. Tracing is something of a mystery. It is a process by which a claim to an asset held by a defendant can be transferred to another asset which the defendant acquires in exchange for the original asset. An example will help. If your trustee, in breach of trust, gives £10,000 of the trust money to Sally, you can, of course, claim against Sally for the return of that money. Having received the money as a gift, Sally is a volunteer (i.e. donee) and thus not a *bona fide* purchaser for value without notice (Section 4.1.1). If Sally spends the money on a car, then you can ‘trace’ from the original £10,000 to the car. Having traced in this way, you can then claim that the car is held on trust for you. Although the rules of tracing are fairly well settled, controversy still surrounds its juridical basis. Since virtually all cases involve a common law tort or breach of trust, some see it as a response to wrongdoing. Others, especially Birks, Burrows, Chambers and Lionel Smith, see it instead as a response to unjust
enrichment. Smith (The law of tracing, 1997, p.357) has observed that trust claims based on tracing are ‘functionally identical to purchase-money resulting trusts’. Others still see it as existing beyond the territory of these nominate heads. Its placement here, in the category of ‘other miscellaneous events’, reflects the uncertainty surrounding it.

19.2.3 Following, tracing, and claiming

It is very helpful to distinguish between following, tracing and claiming. We follow assets, trace value and claim rights. This terminology was used by Smith in The law of tracing (1997) and adopted by Millett LJ in Boscawen v Bajwa [1995] EWCA Civ 15, [1995] 4 All ER 769, [1996] 1 WLR 328. One follows an asset when it is transferred from one person to another. One traces value from one asset to another when the former is exchanged for the latter. One claims rights to the assets that are identified by following or tracing. For example, if, in breach of trust, the trustee gives a painting held on trust to John, the beneficiaries can follow it into John’s hands and make a proprietary claim to it. If John sells the painting for £1,000, they can trace the value of the painting into that money, and likewise claim that the money John received in exchange is held for them on trust. If John pays the money into a bank account, they can trace from the money to the account (i.e. the bank’s debt to John) and say that it is held on trust for them.

The concept of tracing value is useful, but must not be taken too literally. If one asset is exchanged for another, enabling the beneficiaries to claim a trust of the substitute, the values of those assets are not relevant to the claim. For example, if £1,000 of trust money is used to buy a painting, the beneficiaries can claim the painting regardless of its value, even if it turns out to be worth millions: Foskett v McKeown [2000] UKHL 29, [2001] 1 AC 102. See R. Chambers ‘Two kinds of enrichment’ in R. Chambers, C. Mitchell and J. Penner The philosophical foundations of the law of unjust enrichment. (Oxford: Oxford University Press, 2009) p.242.

SELF-ASSESSMENT QUESTION

In breach of trust, Tom transfers £1,000 to Eric which he uses to buy a television. Eric then gives the television to his girlfriend, Padma, who then trades it for a sofa. The beneficiaries sue Padma for the sofa.

Describe the basis of the beneficiaries’ action, using the terms ‘following’, ‘tracing’ and ‘claiming’.

19.2.4 Tracing at common law

Taylor v Plumer (1815) 3 M&S 562, 105 ER 721 is supposed to provide the foundational authority for the common law right to trace (i.e. for the legal owner of an asset to trace its value into an asset acquired in exchange and assert legal title to the new asset), but it does no such thing. It is now generally recognised that the case was decided upon equitable principles: see L. Smith ‘Tracing in Taylor v Plumer: equity in the King’s Court’ [1995] 2 LMCLQ 240. Nevertheless, it appears that the common law can provide the legal owner with a power to assert title in the traceable proceeds (Lipkin Gorman v Karpnale Ltd [1988] UKHL 12, [1991] 2 AC 548). This requires an act on the part of the legal owner, who does not automatically, by operation of law, acquire ownership of traceable proceeds in the way the beneficiary does in equity in respect of the traceable proceeds of trust rights. To the extent that this power to assert title counts as tracing at common law. It also appears that the rules governing tracing through mixtures (discussed below) are less developed at common law than they are in equity.

In FC Jones & Sons v Jones [1996] EWCA Civ 1324, [1997] Ch 159, a trustee in bankruptcy was allowed to trace at common law from cheques drawn on the account of the bankrupt firm and paid into a brokerage account in the name of the wife of one the partners. Millett LJ said (at [28]) that equitable tracing rules should be available in support of the common law claim:  

Go to your study pack and read ‘Property, unjust enrichment, and tracing’ by P. Birks.
There is no merit in having distinct and differing tracing rules at law and in equity, given that tracing is neither a right nor a remedy but merely the process by which the plaintiff establishes what has happened to his property and makes good his claim that the assets which he claims can properly be regarded as representing his property. The fact that there are different tracing rules at law and in equity is unfortunate though probably inevitable, but unnecessary differences should not be created where they are not required by the different nature of legal and equitable doctrines and remedies. There is, in my view, even less merit in the present rule which precludes the invocation of the equitable tracing rules to support a common law claim; until that rule is swept away unnecessary obstacles to the development of a rational and coherent law of restitution will remain.

Summary

Where rights have been transferred in breach of trust, equity allows beneficiaries not only to follow those rights into the hands of third parties (not being bona fide purchasers for value without notice) but to trace the value of those rights into rights received through an unauthorised exchange. After the exercise of tracing, beneficiaries may claim against the persons who hold or held the traceable proceeds of trust rights. The common law has no exact equivalent to tracing, though it does allow title holders to assert a title in the traceable proceeds of rights held at common law in certain circumstances. It is orthodoxy that this power to assert title cannot be exercised following the mixing of the rights in question with other rights.

19.2.5 The rules of tracing

The requirement of a fiduciary relationship

In order for an individual to have the advantage of the equitable rules of tracing, they must normally have an interest under a trust, for it is the value of that right which is traced into proceeds. However, equity is also willing to allow claimants to trace where a fiduciary breaches their duty and in the course of that mishandles their principal’s rights (Re Diplock [1948] Ch 465 (CA), affirmed [1951] AC 251). So, for example, if a company director uses their power to transfer the company’s rights in breach of their fiduciary duties, say by transferring company money to their own bank account, the company will have the advantage of the equitable rules of tracing to trace into any proceeds acquired with that money. Courts have shown themselves willing to find the existence of a fiduciary relationship in order for plaintiffs to apply the tracing rules (El Ajou v Dollar Land Holdings [1993] 3 All ER 717), even where none really existed (Chase Manhattan v Israel-British Bank [1981] Ch 105).

Whole and part ownership

These rules are straightforward. If the trustee takes £500 of trust money and spends it all on a title to a rare book, then the beneficiaries can claim that the book is held for them absolutely. If the trustee uses £250 of trust money and £250 of their own money to buy the book, it will be held by the trustee for themself and the beneficiaries in equal shares (Foskett v McKeown [2000] UKHL 29, [2001] 1 AC 102).

Tracing through mixtures

What happens when the trustee or a third-party recipient of trust rights mixes them with their own so that the original right cannot be identified? The rules have largely developed in the case of a trustee or recipient mixing trust money or its traceable proceeds with their own by depositing it at a bank so as to add to the balance of their bank account, for example, depositing £500 of trust money in their bank account, which has a balance of £250, raising the balance to £750. The first thing to note is that equity does not regard this mixing as giving rise to co-ownership of the chose in action against the bank, as it does in the example of the last section where trust money and the trustee’s money went to purchase a new asset, the rare book. The trust does not have a 2/3 share in the chose in action, the trustee a 1/3 share. Equity seems to hold that the trust money and the trustee’s money remain separately held, though which money belongs to whom is not distinguishable. Because of this, if £300 is withdrawn...
from the bank account by the trustee and spent on title to an armchair, that title is not regarded as co-owned by them in $2/3$ and $1/3$ shares. Rather, equity employs rules to determine whose money was withdrawn and spent to acquire the title. The rules are different when the person who mixes the trust money is a wrongdoer, for example, a trustee in breach or a third-party recipient who takes trust rights in the knowledge that they receive it in breach of trust, from those that apply to an innocent mixer, such as a third-party recipient who does not know that the money was wrongfully taken from a trust.

**The rules governing wrongdoers**

The rules are wrongly seen as a set of evidentiary presumptions. The first presumption is that a wrongdoer who mixes trust money or its traceable proceeds with their own, and then takes money out of the mixture and spends it, is presumed to spend their own money first, so that anything which remains can be claimed by the beneficiaries: *Re Hallett's Estate* (1880) 13 Ch D 696 (CA). However, equity very soon afterward admitted the opposite presumption in *Re Oatway* [1903] 2 Ch 356 where a beneficiary was able to make a claim to shares bought with money first taken from the mixture and where the rest was then dissipated with no traceable product. The explanation traditionally given is that there is a presumption that the trustee always acts in the best interests of the trust beneficiaries. However, that presumption is constrained by another rule, the lowest intermediate balance rule. Say, for example, following the purchase of a worthless armchair, the trustee spends the rest of the money in the account on worthless shares, reducing the balance to zero. The trustee then adds £500 of their own money. The courts have held that the beneficiary cannot claim that the new balance of £500 is theirs. If the trustee spends all the trust money and later replenishes the account, as in this example, it will not be presumed that they were paying back the trust money they took, despite the fact that that is exactly what a trustee who was acting in the best interests of their beneficiaries would do: *James Roscoe (Bolton) Ltd v Winder* [1915] 1 Ch 62 (affirmed in *Bishopsgate Investment Management Ltd v Homan Ltd* [1994] EWCA Civ 33, [1995] Ch 211).

A presumption of honesty does not therefore work. In any case, it is difficult to see why we should be presuming someone to be honest when all the evidence shows the exact opposite. In truth, the only way to reconcile these three cases is not to think of presumptions at all, but in terms of the resolution of evidential difficulties. In both *Hallett* and *Oatway* such difficulties existed. Somebody’s money was left in the account in *Hallett*, while somebody’s money bought the shares in *Oatway*. The difficulty was that the trustee’s wrongful act of mixing made it impossible to tell whose it was. It might have been the trustee’s own money, it might have been the trust money, or it might have been a combination of both. That evidential difficulty having been caused by the trustee’s wrongful act, the benefit of the doubt was given to the innocent party, the beneficiaries. Thus, if it suited the beneficiaries to say that trust money had been spent first, as in *Oatway*, then they could do so. On the other hand, if it suited them to say that the trustee’s own money had been spent first, as in *Hallett*, they could do that as well. But when we get to a case like *Roscoe v Winder* [1915] 1 Ch 62, there is no doubt to resolve beyond the lowest intermediate balance, for we know where the money came from which later increased the balance: from the trustee’s own funds.

**The rules governing innocent persons**

The beneficiary does not get the benefit of any doubt against an innocent person who mixes trust money with their own. The rules attempt to be neutral as between them. However, the traditional rule chosen tends to lead to haphazard results. That rule, drawn from *Clayton’s case* (1816) 8 LJ Ch 256, is the ‘first in first out’ (FIFO) rule, which works exactly as it sounds. Thus, if an innocent recipient added £500 of trust money to their bank account already containing £250, then their money will be spent first. So the innocent recipient will acquire a $5/6$ share of a title to an armchair bought for £300, since all of their £250 was used up in the purchase, and the beneficiary gets a $1/6$ share, since to make up the £300 purchase price the innocent had to draw upon £50 of the trust money. The remaining £450 in the account is all the beneficiary’s, and so if it is spent on worthless shares, they are the beneficiary’s alone. The Court of Appeal in
Barlow Clowes International Ltd v Vaughan [1991] EWCA Civ 11, [1992] 4 All ER 22 recently affirmed the general applicability of the FIFO rule, but it also acknowledged that it can work unfairly, and indeed in that case the claimants were treated as having shares in the entire fund proportionate to their contributions, so that they shared pro rata in the traceable proceeds available.

**Activities 19.1 and 19.2**

19.1 In breach of trust, Thomas transfers £10,000 to Victor, telling him that the money is a birthday present. Victor pays the money into his bank account, raising the balance to £13,000. He then withdraws £5,000 and uses it to buy a title to a painting, now worth £7,000. He next withdraws £4,000, which he spends on a round-the-world cruise. He is then informed of the fact that the £10,000 he received was transferred in breach of trust. He thereupon spends a further £3,000 from the account to buy a car, which has since decreased in value, leaving a balance of £1,000. Advise the beneficiaries of the trust.

19.2 Tara, a trustee of the Adams family trust and also the Khan family trust, improperly withdraws £20,000 from the Adams trust and deposits it in her bank account, raising the balance to £30,000. She then withdraws £15,000 from the account to buy shares which have since doubled in value. She then, in breach of trust, adds to the same account £40,000 from the Khan family trust, raising the balance to £55,000. She then spends £10,000 on shares which have also doubled in value, then £25,000 on a car now worth half that amount, and later £15,000 on her general living expenses. She then adds £20,000 of her own money, raising the balance to £25,000. Advise the beneficiaries of the two trusts.

**Summary**

Equity has developed various rules which allow beneficiaries to trace through mixtures of trust rights with others. Where a wrongdoer mixes trust rights with their own, the beneficiaries are essentially entitled to control the book-keeping. As between mixtures of the rights of innocents, the FIFO rule is the authoritative starting point, though a proportionate share rule may be applied if the FIFO rule would generate unfair results.

**Backwards tracing**

Backwards tracing is the notion that beneficiaries can trace into an asset that was purchased on credit when the provider of that credit is paid off with trust money. Thus, if a trustee or recipient of trust funds buys a car for £10,000 with money borrowed from a bank or with their credit card and then pays off the loan or credit card bill with trust money, can the beneficiaries trace backwards and claim the car as the traceable proceeds of the trust money? Without saying so, English law seems to have allowed backwards tracing in a few cases: *Agip (Africa) Ltd v Jackson* [1990] Ch 265; affirmed [1990] EWCA Civ 2, [1991] Ch 547 (backwards tracing through the bank clearing system); *El Ajou v Dollar Land Holdings plc* [1993] 3 All ER 717 (Ch D); reversed [1993] EWCA Civ 4, [1994] 2 All ER 685 (tracing through credit facilities); *Foskett v McKeown* [2000] UKHL 29, [2001] 1 AC 102 (tracing into payments made on an asset, a life insurance policy that had already been acquired). In the only case which has addressed the issue explicitly, *Bishopsgate Investment Management Ltd v Homan* [1994] EWCA Civ 33, [1995] Ch 211, the Court of Appeal denied that backwards tracing was recognised in English law. This issue will certainly come before the Supreme Court at some stage, and most commentators argue that backwards tracing should be recognised.

**Activity 19.3**

Read *Bishopsgate Investment Management Ltd v Homan* and explain what it decides, assessing whether the reasoning is persuasive.
19.2.6 Proprietary and personal claims reliant upon tracing

Recall the description throughout Chapter 16 of the various forms of proprietary and personal claims that can be made against trustees and third parties in cases of breach of trust. The point of this section is to remind you that in many cases such claims will be reliant upon tracing, because it is only after the process of tracing has been undertaken will it be known whether certain claims arise. So, for example, if the trustee transfers money in breach of trust to a third party, Sam, who adds it to his bank account, any proprietary claim against Sam will involve tracing the trust money into the bank account or into assets purchased from withdrawals from that account. Similarly, a personal claim can be reliant upon the tracing process. Let us say that Sam now draws a cheque for £1,000 on the account in favour of his cousin, Madeleine, telling her that it is a birthday present, and let us further assume that one can trace some of the trust money into that payment. Now assume that Madeleine finds out that the money was wrongly taken from the trust, but decides to spend the money on a holiday to Italy regardless. Madeleine will be liable to a personal claim for her ‘knowing dealing’, as she dishonestly dealt with a trust right, or rather the traceable proceeds of a trust right. That is, although no proprietary claim can arise against Madeleine, for she has spent the trust money, she is personally liable to restore its value to the trust. Unless we had followed and traced the trust rights from the trustee to Sam, and then traced through his bank account into an asset (the cheque) which we followed into Madeleine’s hands, this personal claim could not arise. So remember that although tracing is a process of dealing with rights, it can be an essential feature in establishing personal, not just proprietary, claims.

Armstrong DLW GmbH v Winnington Networks Ltd [2012] EWHC 10 (Ch), [2012] 3 WLR 835, [2012] 3 All ER 425 is an interesting case involving tracing and claiming with respect to European Union Allowances (created by the EU Emissions Trading Scheme) which were misappropriated from the claimant’s carbon emissions account at the German Greenhouse Gas Emissions Trading Scheme Registry and transferred to the defendant’s carbon emissions account at the UK Greenhouse Gas Emissions Trading Scheme Registry. The case discusses the various personal and proprietary claims potentially available at common law and in equity.

The second purpose of this section is to point out the two standard proprietary claims made in respect of traceable assets. Where the traceable proceeds consist of a right that has risen in value, the beneficiary will claim that that right is held for them on constructive trust, because they will then have the advantage of the rise in the asset’s value. Where the asset has declined in value, the beneficiary can decline ownership of the asset, and instead demand repayment of the trust money, with that debt secured by an equitable lien over the asset. An equitable lien is an entitlement to have a right sold to pay off a debt, if the debt in question is not paid off by the debtor.

A lien will be most convenient to the beneficiary in the case where the purchase price of a right that has declined in value is made up of both the beneficiary’s and the wrongdoer’s money. So, for example, consider the case where the tracing rules indicate that £5,000 of trust money and £5,000 of the trustee’s own money were used to purchase a car for £10,000 which is now worth only £7,000. If the beneficiary’s claim an ownership share, they will have a half-interest in the car worth only £3,500. They would be better to forego that right, and demand that the trustee repay them £5,000 from their own pocket (a personal claim against the trustee to restore the trust) and claim a lien on the car to secure that obligation. Thus if the trustee does not pay back the £5,000, the beneficiaries can have the car sold, for £7,000, of which they have the right to £5,000. Thus by foregoing the ownership share they get all their money back.

Activity 19.4

Go back to the fact situations in Activities 19.1 and 19.2 and state the claims that might be made following the tracing process.
19.2.7 Rights to subrogation reliant upon tracing

Subrogation occurs when A acquires B’s rights against C by operation of law. The insurance context provides an illustration: assume that an insurer, A, insures B against negligent injuries by a third party. If C, a third party, negligently injures B, B will have a right to sue C for damages to compensate B for B’s injury. However, when A the insurer pays B an insurance award to cover B’s loss, A acquires by subrogation B’s right of action against C. A is said to be subrogated to B’s claim against C. Similarly, in certain circumstances, if A pays off a debt that B owes C, then A will be subrogated to C’s claim against B which A paid off. In other words, A can now bring an action against B for the amount that B previously owed to C.

The right to be subrogated in such a circumstance can be acquired by a beneficiary if trust money is used to discharge a debt. The trust will be subrogated to the creditor’s right of action against the debtor whose debt was discharged with trust money. This will be particularly useful if trust money was used to discharge a secured debt, such as a mortgage, for there will be subrogation both to the debt and the security for that debt. If, for example, trust money is used to pay off the trustee’s mortgage, the trust will be subrogated to the rights of the mortgage lender, including the right to sell the property and use the proceeds of sale to satisfy the debt if it is not repaid. This may be especially valuable if the trustee is bankrupt, since the charge on the trustee’s house will ensure that the proceeds from the sale of the trustee’s house will go first to paying off the debt owed to the trust.

Activity 19.5

Read Boscawen v Bajwa and explain the decision.

Summary

Backwards tracing is the concept of tracing into an asset purchased on credit where the trust money is later used to pay off that debt. It has not been authoritatively recognised in English law, and the Court of Appeal decision in Bishopsgate was against it, but certain cases can be more easily explained on the basis that the claimant was allowed to backwards trace.

Tracing can be a basis for both proprietary and personal claims. In certain circumstances it may be to the advantage of beneficiaries to claim a charge over the traceable proceeds rather than an ownership share.

Rights to subrogation can arise at the end of a tracing process, and are advantageous where trust assets are used to discharge a secured debt.

Essential Reading

At least one of the following:


- Pettit, Chapter 24: ‘Following and tracing’.


Further Reading

Sample examination questions

Because questions raising tracing issues usually concern breach of trust or breach of fiduciary duty, the questions will usually require you to deal with the law governing liability for those breaches, as the following questions do. Concentrate on the tracing issues for now, but realise that a full exploration of all the relevant issues raised by the question will be required in the examination:

Question 1  Flick is a trustee of two settlements, Settlement No 1 and Settlement No 2. In January of this year, he received a cheque for £10,000, representing dividends from investments in Settlement No 1. He paid this cheque into his personal bank account, which at the time had a credit balance of £5,000. In February, he sold investments forming part of the trust fund of Settlement No 2 for £12,000 and paid this into the same account. In March, he withdrew £15,000 from the account and bought shares in his own name in X Co Ltd. In April, he won £10,000 on the football pools and paid this sum into the same account. In May, he withdrew £12,000 from the account and gambled it away. He has now been adjudicated a bankrupt. The shares in X Co Ltd are currently worth £30,000.

Advise the beneficiaries under each settlement as to their respective claims.

Question 2  Tammy, a trustee, makes the following payments in breach of trust:

a. £5,000 to her niece, Ethel, as a graduation present. Ethel uses the whole of the £5,000 to buy a second-hand car which she could otherwise not have afforded. She soon crashes the car. She receives £4,500 under her insurance policy, the premiums for which she had paid out of her own savings.

b. £10,000 to her accountant Richard to buy shares. Knowing Tammy’s financial circumstances, Richard wonders where the money came from, but does not ask, and buys shares which have since fallen in value to £4,000.
c. £20,000 to pay off the mortgage on Tammy’s house.

d. £5,000 to pay off a credit card bill which Tammy had incurred by buying an antique wardrobe. She still has the wardrobe.

Tammy is now bankrupt. Advise the beneficiaries concerning the liability of Tammy, Ethel, and Richard.

**ADVICE ON ANSWERING THE QUESTIONS**

**Question 1** Flick has mixed money of two different trusts with his own, so that both the rules governing wrongdoers and the rules governing innocents apply. Before the withdrawal in March, the account contains £5,000 of his own money, £10,000 of No 1 money, and £12,000 of No 2 money. The shares in X Co Ltd have doubled in value, so as against Flick, No 1 and No 2 will claim their money made up all of the purchase price. As between No 1 and No 2, they will have shares in the shares either 2/3 for No 1, 1/3 for No 2 on the FIFO basis and 5/11 No 1 and 6/11 No 2 on the proportionate share basis. The £10,000 in pool winnings is Flick’s money, raising his money in the account to £15,000. The beneficiaries will insist that the entire £12,000 dissipated gambling represents Flick’s money, reducing the amount he has in the account to £3,000, out of a total balance of £10,000. The £7,000 will represent money entirely of No 2 if the FIFO rule applies, or a sum shared by them proportionately in 5/11 and 6/11 shares, respectively, if the proportionate share approach is taken.

**Question 2**

a. On orthodox tracing principles, the beneficiaries can trace into the crashed car, which is worthless, but not into the insurance proceeds. True, she would not have purchased the insurance or received the insurance award but for the purchase of the title to the car with trust money, but no trust money was actually used to purchase the insurance policy.

b. The beneficiaries should be advised to claim a charge over the shares for the repayment of the trust’s £10,000, which will provide a better result than claiming a half-interest in shares now worth only £14,000.

c. Following Boscawen v Bajwa, the beneficiaries should be advised to claim to be subrogated to the rights of Tammy’s mortgagee to secure repayment of the £20,000.

d. This part requires a discussion of the possibility of backwards tracing in English law, for if it is available, the beneficiaries can claim that the wardrobe is held for them by Tammy on constructive trust.
Reflect and review

Look through the points listed below.

Are you ready to move on to the next chapter?

Ready to move on = I am satisfied that I have sufficient understanding of the principles outlined in this chapter to enable me to go on to the next chapter.

Need to revise first = There are one or two areas I am unsure about and need to revise before I go on to the next chapter.

Need to study again = I found many or all of the principles outlined in this chapter very difficult and need to go over them again before I move on.

Tick a box for each topic.

<table>
<thead>
<tr>
<th>I can explain how some constructive trusts can be seen as responses to a defendant’s unjust enrichment.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can define the circumstances in which constructive trusts will arise in circumstances which involve neither wrongdoing nor unjust enrichment.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can define the difference between following, tracing and claiming.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain why the law of tracing often falls into the law of constructive trusts.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain when the common law does not allow a title holder to trace.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I understand and can apply the rules governing tracing through mixtures.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can explain what backwards tracing is and why the law regarding it is unsettled.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can outline the proprietary and personal claims that can arise following the tracing process.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>I can show how rights to subrogation can arise following the tracing process.</th>
<th>Ready to move on</th>
<th>Need to revise first</th>
<th>Need to study again</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

If you ticked ‘need to revise first’, which sections of the chapter are you going to revise?

<table>
<thead>
<tr>
<th>Must revise</th>
<th>Revision done</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

19.1 Constructive trusts as a response to unjust enrichment

19.2 Constructive trusts responding to other miscellaneous events
NOTES
Feedback to activities
Chapter 2

**ACTIVITY 2.1**

You cannot be expected at this stage to comprehend all the specific provisions of these instruments; it is useful merely to read through them to get a sense of the large number of considerations which arise in setting up and carrying out a trust – like those who draft contracts, drafters of trust instrument try to anticipate all manner of situations which might arise in the life of a trust and provide the means to deal with them. On point (c), notice that both of these precedents reflect the modern trend of giving trustees numerous wide powers to deal with the trust rights, rather than specifying in detail how they are to be managed and distributed.

**ACTIVITY 2.2**

a. The parties were husband and wife, who both contributed to the purchase of a fee simple title to a family home. The issue was whether there was any basis for altering the co-ownership shares each spouse would normally receive based upon the proportions each contributed to its purchase. The court held that there was not.

b. Briefly, Bagnall J insisted that justice must be determined according to law, which can be attained by mortals who apply rules and principles acquired over time, not on the basis of general considerations of fairness, in particular in respect of property rights, otherwise no lawyer could safely advise their client. It might be unfair, all things considered, for Mrs Cowcher to receive a smaller share of the title than her husband given all she had done for him, but there was no basis in the law of trusts to grant her a larger share for that reason alone.

**ACTIVITY 2.3**

a. In Quistclose, a company to whom money had been lent, was said to hold that money on trust for the lender until such time as it had been used for the purpose of the loan, and in *Re Kayford* a company was held to have established a trust of the advance payments of its customers, which it would hold on trust until those customers’ orders of goods had been filled.

b. The finding of a trust in both cases meant that the lender and the customers were able to claim the return of the full amount of the loan and their pre-payments, respectively, when each of the companies became insolvent – that is, the trust arrangement ensured that they were not merely ordinary creditors who would rank *pari passu* with all of the other ordinary creditors of the companies. This in turn raises the question whether the law of trusts should recognise such arrangements, as they arguably undermine the statutory regime of insolvency.

**ACTIVITY 2.4**

The main point to grasp here is that a trust is not the same thing as an agency, a bailment, a contract, or a debt, but that the trust can be used in combination with many of these other legal devices (in particular trust and contract, trust and agency, and trust and debt), to generate different legal arrangements.

Chapter 3

**ACTIVITY 3.1**

No feedback provided.

**ACTIVITY 3.2**

A typical family trust contains successive and discretionary elements. A successive interest is one taking effect after a prior interest ends. If you are married, then you might typically provide for your spouse for the rest of their life after your death, and leave the remaining funds for your children on your death. So you might put funds on
trust for ‘your spouse for life, remainder to your children in equal shares’. Under those
terms your spouse will get the income from the trust investments as long as they live,
and upon their death, your children, who have the ‘capital’ interest, will be entitled to
the transfer of equal shares in the trust rights. So far, we have a fixed trust. You might,
however, give your trustees a discretion over the income while your spouse is alive, to
give the income to your spouse and/or your brothers and sisters in such shares as your
trustee ‘shall in his absolute discretion see fit’. That way, your trustee can give money
to any of these people according to their current needs. Or you might make the shares
of capital discretionary too, allowing the trustee to appoint the capital on the death of
your spouse in whatever shares the trustee decides. Drafting trusts so as to properly
take into account all future possibilities is a difficult business, and centuries of effort
have gone into refining the structure of trusts to do so. Nowadays, trust instruments
tend to avoid the use of contingent interests, but instead give the trustees very
expansive discretions to add or delete beneficiaries, to vary shares, and so on, so that
the trust can be adapted to changing circumstances.

ACTIVITY 3.3
a. Obviously a discretionary, testamentary trust with a defeating provision
   (establishing a residence outside the UK); clearly a special trust. The gift of capital is
   a public purpose, or charitable, trust.

b. The trust here may appear to be resulting, but the shares awarded by the court
   make it clear that it is not. The ambiguity of the terms ‘constructive’ or ‘implied’
   mirrors the uncertainty whether the trust awarded by the court reflects the
   parties’ intentions or arises by operation law.

c. An express, inter vivos, trust, which is also invalid for being a private purpose trust.

d. An express trust, which fails for uncertainty of objects – an automatic resulting
   trust of the £10,000 to his estate on death.

e. The question is whether there is a resulting trust here.

f. The express trust formed by Fred and Bill with the solicitor is breached by the
   latter. The nephew, who is not a bona fide purchaser, holds the £10,000 on trust for
   Fred and Bill, under a constructive trust arising by operation of law.

Chapter 4

ACTIVITY 4.1
The main points of difference are, regarding bailment: as a transfer of possession,
not title; regarding agency: the relations between the agent and principal here are
personal and contractual, not proprietary. Thus when the agent collects the rent for
P, the agent generally receives the money outright – he merely owes P a sum of like
amount. If the rent money is stolen from the agent, it is the agent’s loss. He still owes
P the same amount. If the agent held the rent he collected on trust for P, then if the
rent money was stolen then it would be P’s loss: Morley v Morley (1678) 2 Cas Ch 2. On
the other hand, if the agent became bankrupt before paying P what he owed, P would
be an ordinary creditor of the agent, whereas if the agent held collected rents on trust
for P, P would be able to claim the rent money as held on trust for him, so avoiding
the effects A's bankruptcy has on mere creditors. As to debt, the relationship between
trustee and beneficiaries is not one of debtor and creditor. The benefit of a debt can,
however, form the subject-matter of a trust.

ACTIVITY 4.2
No feedback provided.
Activity 4.3
A fraud on a power occurs whenever a power, usually a power of appointment, is used to achieve a purpose outside the intended use of that power, typically to benefit some person by a power of appointment who is not a proper object of the power. For example, if a trustee makes a deal with a proper object of a power to exercise the power in that object’s favour, granting him £10,000, if the object agrees to then give £5000 to the trustee, this is clearly a fraud on a power. *Vatcher v Paull* establishes that making the exercise of a power conditional or defeasible on what the proper objects may do does not automatically make the exercise a fraudulent one.

Activity 4.4
a. Trustees can pay as much income as is reasonable, and accumulate the rest; accumulations can be spent in later years during the beneficiary’s minority. Thus, reasonable present needs should be weighed against future needs when more income is likely to be required, and all recurrent expenses (e.g. education, recreation, etc.) should be considered.

b. The main considerations are whether a contemplated advance now would too restrictively curtail future options. Under the Act, only one-half of the beneficiary’s presumptive share can be advanced, though many instruments allow advancements up to the total share, but in either case, present and future needs and opportunities must be weighed against each other.

Activity 4.5
How does the standard apply in dealing with agents in the general course of business, and what phrases does the court use to describe the standard? (*Speight v Gaunt; Re Whiteley*) Does it require the trustee to outperform the market (*Re Chapman*)?

Activity 4.6
Having the power to elect the board of directors, must the trustee elect himself to the board? Insist on minutes of board meetings? Actively direct the company’s affairs?

Activity 4.7
The trustees were in breach of trust for failing to understand the investment clause of the trust instrument, and therefore they invested in a smaller range of securities than they might have done, and yet Miss Nestle’s claim that the 80 per cent fall in the real value of the trust capital failed – was it because the breach did not lead to the loss? Or because the trustees properly favoured the interests of the life tenants (income beneficiaries) or both?

Activity 4.8
Against social investing, one should emphasise that Scargill’s claim was that a trustee should be able to advance the trustee’s ethical commitments via their investment of the trust rights, even against the beneficiaries’ wishes or best interests. In favour, one might say that given the vast amounts held in trust, especially by pension funds, this would provide a means for ethical and moral views to improve business practices in the world of investment banking and finance; secondly, it is not clear that all ethical investment strategies result in reduced returns.

Activity 4.9
Clearly the decision to delegate investment powers turns most importantly on the trustee’s own expertise. To the extent the trustee is not an expert, they must seek expert advice, and for reasons of efficiency in both time and the expenditure of fees, which will depend in part on the size of the trust and the sort of obligations the trust imposes (for example to pay regular income, or rather to accumulate income for a long period) it may be sensible to delegate the power of investment. Of course, before doing so, the qualifications of any proposed agent must be investigated.
Chapter 5

Activity 5.1

a. The plaintiff, Mrs Paul, who had lived with Mr Constance in the last years of his life, claimed against Mr Constance’s widow, who was administering Mr Constance’s estate on his death, that Mr Constance had declared that he held a bank account in his name on trust for himself and Mrs Paul in equal shares, the declaration taking the form of his telling Mrs Paul on several occasions that the money in the bank ‘was as much yours as mine’.

b. The defendant argued that the proper interpretation of the facts indicated that though Mr Constance might have attempted to make a gift of a share of the money to Mrs Paul, he had failed to do so properly, as in Jones v Lock; the court had no power to treat this failed intention to make a gift as a declaration of trust; further, from this principle, the defendant argued that there needed to be a clear intent by the purported settlor to confer rights on a purported beneficiary to count as a declaration of express trust, and here there was none.

c. The Court of Appeal held (1), that there was no question of a direct gift in this case which had failed, as in Jones v Lock, and that, given the unsophisticated nature of the parties, Mr Constance’s expression that the money was as much the plaintiff’s as his own on numerous occasions was sufficient as a declaration of trust. An express trust was therefore found to have been created.

Activity 5.2

No feedback provided.

Activity 5.3

After reading and noting the Court of Appeal’s decision, the difference in approach taken by Megaw LJ and Sachs LJ towards certainty of objects should become clear.

Sachs LJ makes a clear distinction between conceptual uncertainty and evidential uncertainty; the ‘is or is not’ test applies only to the former, and ‘the court is never defeated by evidential uncertainty’. Therefore it is a question of fact whether ‘any individual postulant has on inquiry been proved to be within (the class); if he is not so proved then he is not in it’. However, Megaw LJ introduces a factor of substantial numbers into the ‘is or is not test’. If it could be said with certainty that a substantial number of beneficiaries fell within a class, the class is certain and therefore the trust is valid. However, it gives no guidance to the trustee as to the extent of any survey they must make of the class before distributing (i.e. the extent of the consideration they must give to distributing to those not within the ‘substantial numbers’ yet who may fall within the class intended by the settlor). What is not clear, given that there was conceptual certainty on the facts, is whether Megaw LJ would require this too.

A trust to distribute monies to adherents of the Anglican church might serve as an example of a trust which would fail Sachs LJ’s test but possibly pass Megaw LJ’s – it is not clear that it could be said with certainty of every person whether or not they were within the class (e.g. those who only attend services sporadically) and this is a matter of conceptual, not evidential uncertainty. However, it is clear that on any definition of ‘adherent’, substantial numbers would fall within the class (e.g. all those who are members of the clergy, regular attenders, etc.) and so this trust may pass Megaw LJ’s test. We should note again, however, that Megaw LJ’s comments were made in the context of a conceptually certain trust.

Activity 5.4

‘Conceptual uncertainty’ arises from the settlor’s use of imprecise or vague language in expressing their intentions. Vagueness can be understood as the problem of the uncertain boundaries which arise when we try to apply words to things in the world. For example, the word ‘tall’ appears to have very uncertain boundaries; ‘tall’ is not a synonym for ‘5’10” and over’; it is not that precise. As a consequence, the use of the
word ‘tall’ in a trust would result in the declaration of trust being void for conceptual uncertainty. ‘Evidential uncertainty’ arises when there is insufficient evidence to conclude that an object is within the specified class of objects. The terms of a trust may be conceptually clear, but actually providing evidence to meet them may be impossible.

**Activity 5.5**

Evidential uncertainty defeats a fixed trust entirely. The reason is straightforward: if the settlor expresses their gift in such a way that evidence must be adduced to identify the rights or person and that evidence is not available, the trust cannot be executed according to its terms.

Evidential uncertainty as regards any particular object will not invalidate a discretionary trust, nor a power of appointment. As long as there are objects who can provide sufficient evidence to prove that they are within the class, there will be valid objects under the trust, and it will not fail. If, however, there is no possibility of adducing evidence to prove that anyone falls within the class, then the trust will fail just as in the case of a fixed trust, even if perfectly conceptually certain. Examples of this sort of trust are likely to be fanciful (e.g. a trust for all those persons who had male ancestors in the 16th century with an extra Y chromosome).

**Activity 5.6**

a. When a power is held by a fiduciary, typically the trustee(s) of the trust, the fiduciary cannot release it. Moreover, they will have duties in relationship to it, to consider exercising it from time to time, and so to survey the class and determine whether an appointment should be made, and to respond to requests by particular objects that they be considered; they must exercise the power in a responsible manner for the purposes for which it was given, and in particular must not act capriciously in determining whether and how to exercise it.

b. While Megarry J held that intermediate powers are valid when held by fiduciaries, not being subject to the administrative workability test, which he held applied only to discretionary trusts, nor being capricious, he said that he would probably hold an intermediate trust invalid, on the basis that the duties of a discretionary trustee are more stringent than a fiduciary powerholder and that the beneficiaries of a discretionary trust have more rights of enforcement than objects of fiduciary powers. It is not clear how these differences lead to the invalidity of intermediate trusts, for the enhanced duties of the discretionary trustee are clearly a matter of degree, following *McPhail v Doulton*, and the object’s rights of enforcement do not seem to have anything to do with whether a trustee or donee of a power can carry out a sensible survey of objects and distribute rights responsibly.

**Chapter 6**

**Activity 6.1**

The first point to note is that *Milroy v Lord* establishes the general rule that ‘equity will not assist a volunteer to perfect an imperfect trust’. Consequently the limit placed on the settlor is that, if the settlor attempts to create a trust with a third party as trustee but that trust is imperfectly constituted, the settlor will not by that fact alone become the trustee. The general principle is that the court will not construe a failed attempt to make a gift in one way as an effective attempt in another way, and typically this will mean that the court will not treat a failed gift or a failed attempt to constitute a trust as a self-declaration of trust.

Regarding the limits on the court, you should remember that if the court intervened and imposed a trust on the settlor, it would result in a trust coming into existence which was not one intended by the settlor; it would, in other words, be a constructive trust. However, as you read on you will see that the court has departed from the rule in *Milroy v Lord* in six specific situations.
**Activity 6.2**

a. There are three principal methods by which a gift of the shares and the title to the painting can be made:

1. A transfer of the shares (as choses in action) must be made in the proper manner and the title to the painting by delivery or deed.
2. By you declaring yourself a trustee of the shares and your title to the painting in favour of your friend.
3. Finally, you can transfer the shares and the title to the painting to a third person to hold on trust for your friend. It is these three modes of transfer which the court in *Milroy v Lord* held were mutually exclusive, and, in particular, would not treat failed attempts to transfer the right by modes (1) and (3) above as cases of (2) (i.e. as self-declarations of trust, regarding which you will notice that no transfer of any right is necessary, and is therefore the simplest to effect).

b. Turner LJ in *Milroy v Lord* said that ‘equity will not assist a volunteer to perfect an imperfect trust’. *Re Rose* presents one of six departures from this general rule. But does this departure represent a conflict with the Court of Appeal’s decision in the earlier case? In his leading judgment, Evershed MR certainly did not think it did. He said that Turner LJ’s judgment was only meant to apply where the transfer in question had not been carried out in the appropriate way. This, however, is nowhere stated in *Milroy v Lord* itself. Nor is there any logical reason why it should make a difference. Indeed, it could be said that *Milroy v Lord* tells us that any intervention by the court would result in a trust being created that was not intended by the settlor/donor. Furthermore in both cases the donor had told the donee that the gift was perfect, so this cannot be a distinguishing factor. Thus, despite Lord Evershed MR’s words, there does appear to be a conflict with the previous case.

c. The term ‘unconscionable’, like ‘unfair’ or ‘unjust’ gives little guidance to a court trying properly to characterise the sorts of facts which should cause it to perfect an imperfect gift, for it is a conclusion only. What it fails to tell us is what particular facts lead to this conclusion. Perhaps the most obvious cases occur when the parties have acted on the basis that a gift was valid, and so have detrimentally relied upon it. But it is not clear that the only way to deal with such an occurrence is to perfect the gift, rather than compensating the relying party for their loss, or stripping the donor of any extra advantage they would receive if the gift were now treated as invalid, for example, strip the donor of the value of a house the intending donee built on land which was not properly transferred. Cases such as *Re Rose* and *Pennington* do not, however, present compelling cases of ‘unconscionability’, whatever that word might mean.

---

**Chapter 7**

**Activity 7.1**

No feedback provided.

**Activity 7.2**

No feedback provided.

---

**Chapter 8**

**Activity 8.1**

No feedback provided.
Activity 8.2
The admissibility hurdle in s.9 Wills Act is far higher than that of s.53(1)(b), requiring in addition to the testator’s signature, the witnessing of the signature by two witnesses before the evidence is admissible. The reasons are not far to seek. When the will comes into operation, the testator is dead and can no longer give evidence that the signature was genuinely made in the full knowledge of what they were doing, etc., and so a higher standard of formality to prevent fraud is imposed. Section 15, by avoiding ‘beneficial devises’ to attesting witnesses, ensures that the testimony of witnesses to a will in court, if the will is challenged, is not tainted in favour of the document’s admissibility.

Activity 8.3
Secret trusts are in direct conflict with s.9 because by them, evidence which the legislature has said is not admissible to prove a testator’s will is regularly admitted.

Activity 8.4
This case reveals a clear disparity in the reasoning of their Lordships, some relying on the dehors the will theory, some relying upon a modified fraud theory by which the operative fraud, if evidence of the declaration of trust was not admitted, would be a fraud on the intended beneficiaries. It is obviously a matter of judgment whether the rationales are convincing.

Activity 8.5
As regards the original fraud theory, the disqualifying factors should be judged on the basis of whether deciding the case one way or the other would give rise to a fraud by the trustee. For example, where the secret trustee predeceases the testator, there can be no fraud, so there is no reason to admit the non-conforming evidence. Of course, under the broader fraud theory given voice to in Blackwell, by which the operative fraud is denying the secret beneficiaries the gift the testator intended, any time the evidence is not admitted there is a fraud. Then the court should admit the evidence in any circumstance it can, but of course this theory is circular. On the dehors the will theory, problems can arise with the consistent application of the rules. For example, by that theory one might save a half-secret trust from the application of s.15 where either the secret beneficiary witnesses the will or the half-secret trustee does, but one cannot do so in both cases.

Chapter 9

Activity 9.1
Some commentators say that the judges blindly followed Eve J’s decision, though it arguably went beyond the bounds of the rule that equity will not assist a volunteer. The opposing view is that trustees cannot have any option whether or not to sue to enforce a covenant; either they have the duty to sue to constitute the trust, or no right to do so because equity will not assist volunteers to enforce promises without consideration (whether oral or within a deed) to constitute a trust, and equity will not make a distinction between volunteer trustees and volunteer beneficiaries; a promise to a volunteer is equally unenforceable whether made to a donee directly or to a trustee in a beneficiary’s favour. The fact that the promise is contained in a deed which the law would enforce is immaterial from this perspective: to allow the enforcement of covenants to settle by the trustee would allow the law to determine the constitution of trusts, which is the province of equity.

Activity 9.2
The marriage settlement and the covenants within it may be enforced by the wife, the husband, and any children of the marriage. Those who might otherwise benefit, for example, the next of kin, are not ‘within the marriage consideration’ and cannot enforce the covenants. The covenants are enforceable as soon as they
can be performed, so a spouse who receives after-acquired property which must be transferred into the settlement must do so immediately, and if there are beneficiaries within the marriage consideration equity will look upon that as done which ought to be done and regard the spouse as holding that property on constructive trust as soon as it is received. Interestingly, according to Re Plumptre’s ST, if a right is held on constructive trust by a spouse in virtue of the fact that there are beneficiaries within the marriage consideration, but these persons die before that spouse actually transfers the right to the trustees of the settlement, the constructive trust will disappear and not operate in favour of the next of kin.

**Activity 9.3**

In *Re Basham*, the plaintiff who, with her husband, had helped her mother and stepfather for a considerable period of her life in expectation of receiving the survivor’s property, was able to claim that this detrimental reliance entitled her to the property. Notice that the expectation was of a future gift of property, not the expectation that a past gift was valid and acted upon. In *Eves*, the detrimental reliance consisted in exceptional work in contributing to extensive improvements to the land in question – the plaintiff had been (untruthfully) told by her partner that her name would have been put on the title to the land but for her age, and therefore her reliance contributed to the Court’s holding that there had been a common intention or understanding that her partner held the property for them both, and this entitled her to a share. *Dillwynn* is the classic case of proprietary estoppel. Here there was a genuine attempt to transfer title to the land in question, which was ineffective for want of a deed. The plaintiff expended substantial monies building on the land, and this detrimental reliance on the validity of the original flawed transfer was such as to convince the court that the transfer should now be ordered to be made perfect.

**Chapter 10**

**Activity 10.1**

No feedback provided.

**Activity 10.2**

a. Tax relief to charities is generally based upon the idea that charities provide public benefits; since they are not for the private benefit of individuals or corporations, they should not be subject to the rules of taxation which are meant to raise revenue from private individuals for the running of the state. It is also sometimes claimed that charitable works would have to be provided by the state if charities did not carry them out, so they save the state money. As you will see, however, not all charities provide the same kind of public benefits, and it is arguable that blanket tax relief for them all is not warranted. Finally, countries like the UK have a large charitable sector, which forms a substantial part of the economy, and it is sometimes argued that this economic activity should be taxed in some way, even if not in the same way as the ‘for profit’ sector.

b. The point here is that the forum for determining charitable status should be more democratic; judges might appropriately determine rights under the law, but they have no expertise in drawing fine distinctions between activities that are truly for the public benefit and those which might only appear to be so. Should there be some public body other than the courts which should do so?

c. The point here is that in view of the fiscal privileges, courts tend to be conservative about what counts as charitable, in order to prevent giving charitable tax status to activities which are not clearly for the public benefit – if tax consequences did not follow, then the courts might allow many more ‘not for profit’ purposes to count as charitable.
**Activity 10.3**
The trust was for a working men’s hostel in Cyprus where there was a severe housing shortage. But working men are not all poor, and so it was not clear the trust genuinely relieved poverty. But given the housing shortage, the trust was allowed as charitable under the category of trusts to relieve poverty.

**Activity 10.4**
It is very difficult to distinguish these research cases, since it is not clear that Shaw’s purpose was less beneficial to the public than research to show that Bacon was the author of Shakespeare’s plays.

**Activity 10.5**
No feedback provided.

**Activity 10.6**
No feedback provided.

**Activity 10.7**
No feedback provided.

**Activity 10.8**
No feedback provided.

**Activity 10.9**
a. The question here is whether a general charitable intent is disclosed – *Re Harwood* suggests that it is easier to find a general charitable intent when the named charity never existed than when it once did but is now defunct, on the basis that in the former case the testator’s intention is more general, the specific location not mattering so much to him (otherwise he would have taken more care in naming an actual charitable institution). Do you find this reasoning persuasive?

b. This is not a case of *cy-près*. If one charitable institution’s work is continued by another, the gift goes to the continuing institution as a fulfilment of the testator’s intention, unless there is some indication that the testator would not have favoured this.

c. This might not be a case of *cy-près*. According to *Re Vernon WT*, a gift to a charitable company ought normally to be construed as a gift to the company directly, to carry out whatever charitable activities it does. This reasoning does not seem entirely persuasive, and in appropriate cases one might construe the gift as being for the named charitable purpose, treating it as having failed, and then assessing whether there was a general charitable intent to allow the gift to be applied *cy-près*.

**Activity 10.10**
a. Not charitable – clearly political.

b. Probably not charitable, for failing the public benefit test because of the restrictions to children of the corporation – the preference may possibly save it – see *IRC v Educational Grants Association Ltd*.

c. Almost certainly not charitable as actually being against religion, and perhaps political as well, despite the fact that the research, if it could be carried out, would be enormously significant.

d. The actual educational purpose is charitable, but is almost certainly tainted by the association with a political party; the court would probably rightly fear that this amounted to propaganda masquerading as education.

e. If restricted to students, this would almost certainly be charitable, but see *IRC v City of Glasgow Police Athletic Association*. 
f. This is charitable.

g. May perhaps be charitable – the restriction to relatives does not violate the public benefit test (Re Scarisbrick); the question is whether ‘lacking ordinary comforts’ amounts to poverty.

h. Not charitable, for being a political purpose; see A-G v McGovern.

Chapter 11

ACTIVITY 11.1
No feedback provided.

ACTIVITY 11.2
As possible non-charitable purpose trusts, you might consider certain political activities, such as campaigning against the building of a motorway through a woodland; or activities such as providing buildings and continuing maintenance thereof for a private association such as a cricket club. Parts (a), (b) and (c) all concern how you ought to regard the factual beneficiaries of your trust purpose: would they necessarily have the time or interest in enforcing the trust against the trustee, and should they have any equivalent to Saunders v Vautier rights (Section 4.6.4) to vary the trust, or collapse it, distributing the property amongst themselves?

ACTIVITY 11.3
No feedback provided.

ACTIVITY 11.4
a. Traditional purposes were the education, maintenance (providing for the housing and feeding) or advancement (providing for a position in life, a church living or an army commission) of the settlor’s children.

b. The difficulty is distinguishing a true Sanderson-type limitation on the amount the beneficiary is to receive from the case where the settlor merely expresses a motive for the gift of an entire fund. The practical difference is important, for if all of the funds are not required to meet the cost of the named expense, then in a Re Sanderson trust these funds will not belong to the beneficiary, but to a person who receives a gift of the remaining funds, or on resulting trust.

ACTIVITY 11.5
This requires an overview of the various reasons in favour of and against the law’s upholding private purpose trusts. As we have seen, the main difficulty is in ensuring that there are persons who can enforce the trust against the trustee. Does it matter, in your opinion, that those who can enforce the trust need not do so if they do not want to? For example, would it have mattered if the employees in Re Denley had not wanted a recreation ground, and left the trustees to use the title to land in other ways? Does legislation creating enforcers with a duty to enforce the trust which is itself enforced by the criminal law (as in the Cayman Islands) appeal to you? Should the state be concerned to enforce purposes which are not ‘public’ (i.e. charitable) purposes?

Chapter 12

ACTIVITY 12.1
The case concerned the presumption of advancement and the evidence required to rebut it. It was proved by evidence that a father and son had both contributed to the purchase price of a title to land which was taken in the son’s name. The presumption of advancement was rebutted and a trust in favour of the father was established.
because, in the court’s view, putting the house in the son’s name alone could be explained because it made mortgage financing easier, and in addition, at one point the father’s solicitor drew up a declaration of trust which formally declared that each held a share in proportion to their contributions, though it was never executed. Furthermore, as the father was only 63 and in good health, there was no obvious reason to make a gift to his son of a large share in the house in which the father intended to live.

**Activity 12.2**

The one who advances purchase money has the advantage of the presumption – it falls to the title holder to adduce evidence inconsistent with the making of a declaration of trust, and where, as in this case, no such evidence is adduced, the presumption settles the issue.

**Activity 12.3**

The Court of Appeal approached the case as one of a gratuitous transfer resulting trust (the first situation as described in Section 12.1.1), and held that Mr Vandervell had not adduced sufficient evidence to rebut the presumption of resulting trust. This approach was disapproved in the House of Lords, where their Lordships treated it as a case of Situation 3, an automatic resulting trust arising on failure to specify any objects. The House saw no need or room to invoke any presumption, for there was no gap in the evidence.

**Activity 12.4**

In *Westdeutsche Landesbank*, Lord Browne-Wilkinson said that automatic resulting trusts arise on the basis that the settlor is presumed to intend that the trust assets will come back to them if their intended gifts for some reason fail (e.g. uncertainty of objects) and that in certain cases a settlor might wish instead for the rights to go to the Crown as *bona vacantia* (goods without an owner) if their intended gift fails. The obvious problem with this view is that it is not true that settlors regularly entertain any such intentions, and the automatic resulting trust is applied regardless. Lord Millett might say in reply that we can ‘presume’ that this is what settlors would have wanted had they addressed their minds to the issue, but the courts on a number of occasions, most especially in *Gissing v Gissing*, have said that it is not legitimate for the courts to create trusts in this way.

**Chapter 13**

**Activity 13.1**

Given the fact that the gift was expressed to be ‘in memory of his late wife’ and to be used ‘solely in the work of constructing new buildings for the Association and/or improvements to the said buildings’, it is difficult not to conclude that the testator’s intentions, as expressed, indicated that he wished his money to be devoted to a particular purpose and no other, a purpose (especially considering the ‘improvements’ provision) that might clearly extend beyond any valid perpetuity period.

**Activity 13.2**

Oliver J reasoned that (a) as a valid gift may be made to an unincorporated body as a simple accretion to the funds, so (b) why should a gift specifying a purpose be invalid? The members could, exercising their contractual rights, either enforce the purpose or not as they chose. In this respect, he appeared to adopt the bare trust/contractual mandate construction. However, Oliver J also considered that the expressed purpose could be treated merely as a motive for the gift, not as a trust obligation. Finally, he felt that *Re Denley* was ‘directly in point’, and that the gift could be held valid on the authority of that case.
Activity 13.3

Goff J in Re West Sussex clearly followed the earlier line of cases and not the contract-holding theory. He regarded the purpose trust as at an end when the association was dissolved, and so the members had no rights to the funds. This approach was somewhat contradicted by his apparent admission that had the members chosen to distribute the funds to themselves, defeating the purposes for which the money was held, before the association was dissolved, they might have done so. But this makes little sense, for if the funds were beneficially theirs to deal with prior to the dissolution, then they remained theirs afterwards, for the dissolution of their contractual relations forming the association could do nothing to alter their rights to the fund. In Re Bucks Constabulary Fund, a case with almost identical facts, Walton J found himself 'wholly unable to square' the decision of Goff J in West Sussex 'with the relevant principles of law applicable'. He applied the modern contract-holding analysis. There being no contrary provision in the contract of membership, the members of the Bucks fund were entitled to it in equal shares.

Chapter 14

Activity 14.1

a. as regards replacing a trustee, s.36(1)

b. as regards adding and additional trustee, s.36(6)

c. as regards retiring from the trust, s.39(1).

Activity 14.2

The essence of the decision lies in the nature of the rule in Saunders v Vautier: beneficiaries can collapse the trust, but cannot 'micro-manage' the trust by directing the trustee as to how they should use their powers. If the power to appoint new trustees is given to the trustee, the beneficiaries cannot insist that the trustee make the appointment the beneficiaries favour; that would defeat the point of there being a trust at all. Of course, the beneficiaries can if they wish bring the entire trust to an end, and set up a new trust with a trustee that they prefer, but the beneficiaries cannot make a trustee who is properly exercising trustee's judgment adopt the beneficiaries' views over their own as to the proper administration of the trust.

Activity 14.3

a. This is clearly a breach of fiduciary duty, as the choice of trustee is in Stella's interest, and perhaps indirectly in the trustees' interests, not in the interests of the beneficiaries.

b. Although a difficult situation, if Simon believes that he cannot effectively act in the beneficiaries' best interests, he should retire.

c. Another difficult situation. If Sam is acting in the best interests of the beneficiaries, his use of the power is not an abuse of his fiduciary position; however, if he removes the trustee in order to preserve or enhance his own position in the company, it would amount to a breach.

d. The question here is whether Arthur is properly exercising his discretion; 'because the beneficiaries asked me to' is not a valid reason. If, however, the beneficiaries' request reflects good reasons for his retiring, then his retirement may be acceptable.

Activity 14.4

As the beneficiaries can be expected to look out for their own interests in exercising the power, and there is no one else's interests they ought to consider, this would not appear to be a fiduciary power.
**Activity 14.5**
The court will look to the wishes of the settlor, if ascertainable, will not make appointments which favour some beneficiaries over others, and will in general make an appointment which will further the proper execution of the trust.

**Activity 14.6**
The scope of the court’s jurisdiction to intervene is broad – it can remove or replace trustees if the proper execution of the trust is threatened. The main criterion must always be the welfare of the beneficiaries, though mere friction between the trustee and the beneficiaries is not by itself a ground for replacing the trustee.

**Chapter 15**

**Activity 15.1**
No feedback provided.

**Activity 15.2**
Try to articulate in summary form Denning LJ’s sense that the court’s inherent jurisdiction is actively facilitative (a kind of approach you may recognise having studied other of his lordship’s decisions in other subjects on the course). Does Denning LJ set any reasonable bounds to what he thinks the court ought to be able to do when considering whether to allow a variation? Lord Simonds LC is clearly more concerned that the court does not take it upon itself to re-write settlements just because it might be beneficial so to do. He is also much more concerned that the law develop piecemeal over time, rather than founding the scope of the court’s inherent jurisdiction on a broad, abstract principle of ‘doing good’ for the beneficiaries. In answering the final question, it is worth putting yourself in the position of a settlor, and asking yourself whether you would fear a broad inherent jurisdiction, worrying that a court might, for reasons you would not appreciate, depart from the structure of the trust and frustrate what you had tried to do, or whether you might welcome a broad inherent jurisdiction, putting your mind at rest, for any unforeseen difficulties could be properly sorted out.

**Activity 15.3**
The court’s inherent jurisdiction with regard to the variation of administrative powers is restricted to emergency situations, and the Trustees of the British Museum could not argue that an extension of their investment powers was necessary to prevent an emergency. But as it was sensible and expedient, the court could allow the variation under s.57.

**Activity 15.4**
The Act requires any ascertainable contingent beneficiary who is *sui juris* to consent to a variation even if the likelihood of their becoming entitled to a benefit under the trust is slight; as a result, many individuals who have no real interest under the trust must be found and properly advised in order for a variation to proceed, which can cause substantial cost and inconvenience. The situation is no different than it would be under the general law principle in *Saunders v Vautier*, but the possibility of such cases suggests that the Variation of Trusts Act 1958 should have allowed courts to consent on behalf of such beneficiaries.

**Chapter 16**

**Activity 16.1**
a. A trust is specifically enforced when the trustee has failed to administer the trust or pay income or transfer capital to the respective income and capital beneficiaries. Here the beneficiaries will apply to the court and the court will order the trustee to
carry out the trustee’s duties or replace the trustee with a trustee willing to do so. In doing this, the court has ordered specific performance of the trust.

b. A trustee is personally liable to the beneficiaries when the trustee has to pay money out of their own pocket to compensate for a loss to the trust.

c. ‘Proprietary’ liability indicates the case when the beneficiaries can claim that some specific right the trustee holds is a ‘trust right’, and so must be held as part of the trust fund rather than as the trustee’s own.

**Activity 16.2**

The account is falsified if the trustee has entered into a particular unauthorised and identifiable transaction. Consequently the beneficiaries will apply to the court and call for the trustee to account for this transaction. The beneficiaries will ‘falsify’ the account in respect of that transaction and the trustee will either have to reverse the particular transaction or be personally liable to pay the equivalent sum, plus interest, from their own pocket to the trust. By contrast, the beneficiaries surcharge the account when the trust has less value than it should, but not because the trustee has entered into a particular identifiable transaction. This generally occurs when the trustee has negligently invested trust funds or when the trustee has failed to insure the trust rights and a loss has occurred.

**Activity 16.3**

a. The account would be falsified when the trustee has used trust rights to purchase some rights for themself, for example, a title to a car. The beneficiaries would apply to the court and the trustee may either reverse the transaction or pay the money back into the trust fund out of their own pocket.

b. The account would be surcharged when a trustee has failed to invest in stocks and shares with sufficient care and consequently a loss has occurred. Another example would be failing to insure the trust rights and later a loss of the subject-matter of those rights occurs.

**Activity 16.4**

The main point to explain is that the breach (wrongly paying away the trust money before the conditions were met for its release) did not cause all the loss suffered by AIB. While certainly a breach, it alone did not generate the loss, most of which was called by AIB’s own decision to make a loan of that size to a couple in financial difficulties. If the defendant solicitors had performed the trust properly, AIB would have suffered the same loss except for the £300,000 the solicitors wrongly paid to the couple and for which they already admitted liability.

**Activity 16.5**

Lord Hutton lays out three possible tests for dishonesty which might apply to the case of a third party dishonestly assisting in a breach of trust:

1. a purely subjective test, sometimes called the ‘Robin Hood’ test, whereby a person will only be dishonest if they transgresses their own personal standard of dishonesty, irrespective of the views of honest and reasonable people; this standard has not been adopted by the courts

2. a purely objective test, whereby a person is dishonest if they fail to act to the standard expected by honest and reasonable people, irrespective of whether they themselves do or do not appreciate they are acting dishonestly

3. a combined test, whereby a person is found to be dishonest if they transgressed the standard of honesty as determined by the views of honest and reasonable people, and the person realises that they have breached that standard.

The combined test clearly sets an additional element to be proved by the claimant – while on the facts one might properly infer the self-conscious dishonesty of the defendant, merely showing that the objective standard of honesty was breached is not
sufficient – there must be some basis for showing the defendant appreciated he was acting dishonestly, and furthermore, the defendant may lead evidence to show that he did not fully appreciate that he was acting dishonestly. Lord Millett is harshly critical of applying the combined test in civil cases; while that test might be appropriate for criminal liability, where arguably mens rea is of the essence of liability, it is not justified in cases of civil liability in which victims of breaches of trust ought to be able to expect that those people who act dishonestly on an objective standard should compensate their victims. It should be noted that Lord Hutton and Lord Millett interpret Lord Nicholl’s speech in Royal Brunei Airlines to very different effect, each arguing that the test they favour truly represents the test outlined by Lord Nicholls. It should also be noted that Lord Hutton’s approach is not applied by the Privy Council in Barlow Clowes, the question then being whether we have returned to the dissenting opinion of Lord Millett in Twinsectra. For a recent discussion of this issue in the Court of Appeal, and an examination of the problems English courts face from the point of view of precedent, see Abou-Rahmah v Abacha [2006] EWCA Civ 1492; [2007] Bus LR 220.

**Activity 16.6**

Although the first painting was placed on Ted's wall, Ted of course continued to hold the title to it in trust. As to the second, Ted is personally liable. By selling the title, he has caused a loss to the trust and so he must pay its value plus interest back into the trust. The facts do not indicate what Ted did with the £2,000 he received for selling the title to the second painting, but if he retains it, the beneficiaries have a proprietary claim to it, and if he purchased any traceable rights with the money, they have a proprietary claim to those. Regarding Ted's unauthorised investment, Ted is strictly personally liable for this breach of trust. He is not relieved of this liability because he sought the advice of a solicitor, unless (recall Section 4.5) he is regarded as having properly delegated the investment of the funds to Alex. If Ted is not regarded as having delegated the decision to Alex, he can bring an action for damages for negligence against Alex (making Alex personally liable to him, that is to say, Ted, for his loss (Ted’s own liability to the trust fund)). If he is regarded as having properly delegated the decision to Alex, then Ted will not himself be personally liable to restore the trust, for the loss was not caused by any breach he committed, but he will have a right of action on behalf of the trust against Alex to pay damages for his negligence, and the damages he receives will hold on trust for the beneficiaries. Ted must pursue this claim against Alex, and if he fails to do so the beneficiaries can apply to the court for an order of specific performance to make Ted bring the action against Alex. Alex was negligent but not dishonest in misconstruing the trust terms, so he is not personally liable to the beneficiaries, though as we have seen he is liable for his negligence as outlined above.

With regard to the transfer of £50,000, Ted is clearly personally liable. There is nothing on the facts to indicate that Alex was either negligent in carrying out this transaction, or did so knowing or suspecting it was in breach of trust, so he is not personally liable for dishonest assistance. Alex would not be liable to the trustees, but instead is liable to Ted for his professional negligence. With regard to Alex’s assistance in the transfer of monies to Barbara, much would turn on his level of involvement in the transaction. If Alex dishonestly assisted in the breach of trust he would be personally liable to the beneficiaries to restore the trust to the value it was before this transaction. However, if he was simply negligent, then the beneficiaries will have no claim against him. Barbara is a volunteer recipient of the £50,000. If she retains any of the money or its traceable proceeds, the beneficiaries will have a proprietary claim against her. As to her personal liability, she will only be liable, following Re Montagu, if she had some degree of knowledge that the money was given to her in breach of trust, or following Akindele, it would be unconscionable not to pay back its value (whatever ‘unconscionable’ means). Finally, one might consider whether she should be personally liable on an unjust enrichment basis to repay an equivalent sum to the trust in order to reverse her unjust enrichment at the beneficiaries’ expense.

With regard to the receipt of title to the first painting, there can be no proprietary claim against Fred, because, having dissipated the proceeds of sale, there are no traceable proceeds. Fred, like Barbara, is another volunteer recipient and so Re
Montagu, Akindele, or the unjust enrichment approach would apply to determine his personal liability. Fred may be able to advance the ‘change of position’ defence as he relied on the validity of the gift to sell it and spend the money on a ‘lavish’ birthday party for his wife, which he might well not have done had he not received the title in the first place.

**Activity 16.7**

This is perhaps the biggest issue in the law of trusts at present. Until the House of Lords establishes in a clear fashion the principles of personal recipient liability, controversy will remain. The unconscionability test set down by Nourse LJ is the weakest contender, for it seems positively to embrace uncertainty. ‘Unconscionable’ does not mean anything specifically, as ‘dishonest’ does, and for that reason was rejected as a touchstone of liability in *Royal Brunei*. The remedy appears largely discretionary on this test. While imperfect, the Montagu test does give some guidance as to the requirements of knowledge. The challenge posed by the unjust enrichment approach lies in the intuition that the recipient should not be enriched at the beneficiaries’ expense. Between those two, the obvious result at first glance is that the recipient should pay back the value to the trust. Notice that the unjust enrichment approach does not disregard the defendant’s knowledge entirely – rather it restricts the issue of dishonesty to the application of the change of position defence. Only an innocent recipient can claim change of position.

While the unjust enrichment approach clearly has its attractions, not all are convinced. Smith (‘Unjust enrichment, property, and the structure of trusts’ (2000) 116 LQR 412) points out that cases of recipient liability are not really two-party situations where value is transferred from the beneficiaries to the third party, as when you pay your gas company twice by mistake, in which two-party case the unjust enrichment principles developed and are most clear; they are three-party situations – the trustee, who as a conceptual feature of the trust is interposed between the beneficiaries and the recipient, makes this a three-party situation.

Do the unjust enrichment rules straightforwardly apply where the settlor by creating the structure of the trust also creates the possibility that the trustee may breach the trust? In other words, do the beneficiaries deserve the same sympathy as the person who mistakenly makes a payment? Furthermore, the law provides the beneficiaries under a trust with better remedial rights than the mistaken payer in certain respects: they, but not the mistaken payer, can both follow and trace the trust rights so as to make proprietary claims against the recipient. Perhaps equity has struck a proper remedial balance, giving the beneficiaries extensive proprietary rights against recipients, but limiting them, when those rights run out, to a more limited personal liability which depends on the recipient’s knowledge.

**Chapter 17**

**Activity 17.1**

At a simple level, the fiduciary (the trustee) should not use the trust funds in such a way as to further their own interests. More specifically, there is a conflict because the buyer of the shares, the trust, would like to buy the shares at the lowest possible price, whereas as seller of the shares, the trustee wants the highest price he or she can get for them.

**Activity 17.2**

First you should explain as clearly as you can the facts, and in particular the various different ways in which Boardman acted in consultation with the trustees – was it right to say that Boardman was a fiduciary to the beneficiaries in the first place? Then you should turn to the views of the individual judges. Lords Guest and Hodson said that Boardman placed himself in a fiduciary position by his close association with the trustees in respect of their carrying out the trust, and relying on the foundational case
for the rule, Keech v Sanford (1726) Sel Cas 1 King 61, held he was liable to disgorge any profits made in the course of acting as a fiduciary. Lord Cohen’s view was more subtle: he said that Boardman was in a position of conflict of interest because, having become interested in purchasing shares of the company himself, could not have disinterestedly advised the trustees about purchasing more shares for the trust. Lord Upjohn’s dissent focuses on the harshness of the result, stating that the rule about a fiduciary’s placing themself in a position where their interests may conflict with those of their principal must be reasonably applied, and the conflict was really only fanciful on these facts. A stringent application of the rule can be justified on the basis that fiduciaries must be kept to the highest standards of loyalty, and that if the rule is applied more sensitively or ‘contextually’, it would lose its prophylactic force – it would require judges to make difficult judgments in every case in trying to measure whether the conflict of interests, based upon the parties’ expectations and so on, was substantial. The reality of many situations, where minor conflicts of interest are common, weighs in favour of a more sensitive application of the rule – the decision in Boardman does seem harsh.

**Activity 17.3**

The self-dealing rule is one of the most stringently enforced of all the rules that apply to a fiduciary (see Re Thompson’s Settlement), and the relaxation of this rule in Holder v Holder should be seen as exceptional, based on the special facts of the case: the court treated the defendant as if he were not, in substance, a trustee. Furthermore, Harman LJ in particular pointed out that the purpose of the rule, to prevent the fiduciary from acting as both vendor and purchaser, would not be fulfilled by applying the rule in this case, for the sale of the property was entirely arranged by two executors who proved the will, the defendant taking no part on the vendor’s side of the transaction.

**Activity 17.4**

a. The self-dealing rule applies to this transaction as the trustee has sold her own rights, the shares in XYZ plc, to the trust.

b. The fair-dealing rule applies to this transaction because the agent has attempted to purchase his principal’s rights, the antiques business.

c. Here the trustee is buying the beneficiary’s future trust income, which is an interest, and consequently the fair-dealing rule applies to this transaction.

d. Clearly in this situation neither rule applies as the purchase of the title to the painting is completely separate from the divorce proceedings in which the solicitor was a fiduciary to Jonah.

e. The director is a fiduciary of the company; though the director is selling her own rights to ABC Ltd it is clearly a self-dealing transaction.

**Chapter 18**

**Activity 18.1**

In Lister v Stubbs, Stubbs’ liability for breach of fiduciary duty was treated as a purely personal obligation to pay over the value of the commission, or bribe; he was in the position of debtor to his principal for that amount. Lindley LJ insisted upon the distinction between ownership and obligation, but it is not entirely clear how he would have applied the distinction in other cases of unauthorised profits. Presumably the court did not reason simply that because the money had never been Lister’s, that resolved the constructive trust issue. One assumes that the court would have required Stubbs to hold on constructive trust dividends on shares owned by Lister that Stubbs received as his agent and wrongly dealt with to his own advantage, even though prior to Stubbs’ receipt those dividends formed no part of Lister’s property. In terms of a trust situation, dividends are not trust property before they are received by the trustee, but because such income is payable by virtue of the holding of the capital, and that belongs to the trust, so should the dividends when they are paid.
The point then is that certain payments that were never the principal’s before the fiduciary received them should be held on constructive trust if intercepted by the fiduciary, so a simplistic ‘no constructive trust unless the property was taken from the principal’ reading of the ownership/obligation dichotomy is flawed. Indeed, treating income as the principal’s property gives effect to the ownership/obligation distinction, for as the example of share dividends shows, some payments ‘belong’ to the principal as owner though they were never part of their worldly goods before, because they arise as income on some of the property the principal owns. Of course a bribe or a sales commission cannot be treated in this way, so the decision in Lister seems firm.

Regarding Lord Templeman’s decision in Reid, following the same reasoning it is one thing to require a fiduciary to hold on constructive trust a profit gained at the expense of the trust, for example intercepting income as it is paid, but something else to impose a constructive trust on any profit acquired in breach of fiduciary duty. This distinction seems to be missed by Lord Templeman when he quotes approvingly the extra-judicial writing of Sir Peter Millett (as he then was), who argues that in the eyes of equity the fiduciary receives all payments as if they were intended for their principal. Arguably this simplistic view leads to injustice. For example, if the constructive trust result is applied to Boardman, then the trust acquires a better claim than all of Boardman’s other creditors to rights which were acquired through no loss to the trust, and which was fully paid for by Boardman – he did not just receive the rights from a third party. This seems difficult to justify.

Chapter 19

Activity 19.1

This question involves tracing between innocents, the beneficiary and Victor, to begin with, and then, if the proportionate share rule is applied to tracing amongst innocents, between a wrongdoer and an innocent, after Victor finds out the money was trust money. On the ‘first in, first out’ rule, Victor spends the £3,000 of his own money that was in the account at the beginning plus £2,000 of trust money to buy the title to the painting. The rest of the money is trust money, going on the cruise, which provides no proceeds, and into the traceable proceeds of the car. The remaining money in the account is the trust’s. If a proportionate share rule is adopted between innocents, 10/13ths of the value of the title to the painting is the trust’s, as is 10/13ths of the remaining £8,000, and then of the £4,000 that remains after the cruise expenditure. Victor is now no longer innocent, and so the beneficiary has the advantage of the Re Hallett’s and Re Oatway rules; consequently, the beneficiary can claim that all of Victor’s money (3/13 x £4,000 = £923) went to buy the title to the car, which has decreased in value, although the remainder of the £3,000 purchase price must be trust money, but the beneficiary can claim the entire £1,000 balance that remains in the account.

Activity 19.2

This is a question involving tracing between a wrongdoer and two innocents. As between the innocents themselves, the rules governing tracing between innocents apply, and as between the innocents, whether singly or together, and the trustee, the rules dealing with wrongdoers apply. The first transaction following mixing is the purchase of the shares; here only the Adams trust and the trustee are involved, and the trust will choose to say that the entire purchase was funded with trust money, for the shares have doubled in value. The Khan money is now added, so the account stands £10,000 to the trustee, £5,000 to the Adams trust, £40,000 to the Khan trust. First, assume the ‘first in, first out’ rule for innocents is applied.

The innocents will want to claim the value of the second share purchase, as, like the first, it has risen in value. The £5,000 Adams trust money is spent first under the rule, plus £5,000 of the Khan money to make up the purchase price. The account now stands £10,000 to the trustee, £35,000 to the Khan trust. There is no more mixing of
the innocents’ monies. The car has declined in value, some money has been expended on
traceable proceeds, and £5,000 of money which might represent trust money
remains in the account; under the lowest intermediate balance rule the Khan trust
cannot benefit from Tara’s addition of her own £20,000 at the end, unless there is
evidence she did so to restore the trust, and there is no such evidence. The Khan trust
will require all of the £5,000 in the balance to represent trust money, £25,000 of the
money spent on the car to have been trust money (though it has declined in value,
the only other alternative is the money spent on living expenses which generated no
traceable proceeds) and £5,000 of the trust money to have been dissipated on general
living expenses. All of Tara’s £10,000 is treated as having been dissipated. If we apply
the proportionate share rule, the Adams trust will have a 1/9 share, the Khan trust an
8/9 share in the £45,000 of trust money in the account immediately after mixing. They
will then apply the rules together against Tara, taking proportionate shares in the
entire value of the second share purchase, in the £5,000 balance in the account, in the
entire value of the car, and £5,000 of the money dissipated.

**Activity 19.3**

At first instance, Vinelott J was willing to allow backwards tracing in limited
circumstances, more specifically, when the trustee purchased a right on credit with
the intention of later paying off the credit advance with trust money. This seems
flawed in principle, for intention should not determine where traceable proceeds
arise; what should be determinative is simply which money was used in which
transaction. Nevertheless, in the Court of Appeal, Dillon LJ accepted this limited
form of backwards tracing. Leggatt LJ, on the other hand, rejected the possibility of
backwards tracing outright, on the basis that it was inconceivable that a claim could
be made to an asset acquired before any trust money was misappropriated. But this
claim of inconceivability is unfounded – the whole system of credit operates on the
basis that assets are acquired on the expectation of later money to fund the purchase.

**Activity 19.4**

In the first situation involving Victor, the beneficiary will claim a share under a
constructive trust of the title to the painting, as it has risen in value. If ‘first in, first
out’ rules are applied, then the beneficiary will claim that the title to the car is held
for him on constructive trust absolutely and the balance of £1,000. There is no point
in merely charging the car, for the beneficiary has the full interest in it anyway. For the
money lost through the decline in value of the car and that dissipated, the beneficiary
can bring a personal action against Victor to restore the trust, as he made those
expenditures dishonestly. If the proportionate share rules apply, the only difference
will be that the beneficiaries will charge the title to the car with the repayment of their
money, rather than taking a proportionate constructive trust interest.

In the second situation involving Tara, the Adams trust will claim that the shares are
held for them on constructive trust, as they have risen in value. Tracing between
innocents under the ‘first in, first out’ rules, the two trusts will claim interests under
constructive trusts of the second lot of shares, as they too have risen in value. The
Khan trust will claim an interest under a constructive trust of the title to the car, as
though it has declined in value it was purchased entirely with trust money so there is
no advantage in foregoing the trust interest and charging the car instead. The value
lost on the decline in the value of the car and through dissipation can be claimed
against the trustee personally. On the proportionate share analysis, the trusts will
claim a shared entitlement under a constructive trust in the second lot of shares,
and in the car – there is no advantage in charging the car, for as innocents they must
act together, and one cannot have the advantage of a charge as against the other
innocent. The advantage of a charge only operates where the wrongdoer contributes
to the purchase price, such that a charge will operate to their disadvantage. Again, the
beneficiaries can claim personally against Tara for the trust value which has been lost
and cannot be recovered by claiming ownership shares in the purchased assets.
**Activity 19.5**

The defendant Bajwa intended to sell his mortgaged title to land, and immediately following the sale Bajwa would normally have been required to use the sale money to discharge the outstanding amount of the mortgage debt. The purchase money was raised by the intending purchasers from a different, second, lender who, of course, required that a mortgage on the land was obtained in its favour when the purchase went through. The purchase money was transferred into a solicitor’s client account (which is a trust account) in advance of the purchase. By mistake, and in breach of trust, the money was advanced before the title to the house was transferred, Bajwa using the money to pay off the mortgage. As a result, Bajwa ended up with a clear title to his house, without a mortgage, and the second lender had advanced its funds and received no mortgage in return. The Court of Appeal held that the second mortgage lender was entitled to be subrogated to Bajwa’s lender’s mortgage on the land which its money had been used to discharge.